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Banking in  
Russia, Austro-Hungary  
The Netherlands  
and Japan



Washington : Government Printing Office : 1911

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# Organization of Banking in Russia

BY

PROFESSORS IDELSON AND LEXIS

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[From Conrad's *Handwörterbuch der Staatswissenschaften*, 3d edition]

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# ORGANIZATION OF BANKING IN RUSSIA.

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## I.—HISTORY PRIOR TO 1860.

Banks came into existence in Russia in the eighteenth century through the action of the Government. In the years 1729-1733 the mint received funds from the imperial treasury for the purpose of granting short-term 8 per cent loans on the security of the precious metals. In 1754 the Government established three banks, which were to carry on business not only with the capital assigned to them by the State, but also with the deposits of private individuals. Two of these were to be banks for the nobility, located, respectively, at the old and new imperial residences (Moscow and St. Petersburg), which were to loan money on the precious metals and on precious stones, and to grant credit on the security of mortgages on estates cultivated by serfs. The third institution was

to be a commercial bank for the merchants of St. Petersburg. The finances of these institutions became embarrassed through mismanagement, and in 1782-85 they were successively closed. In 1757-58 the Government undertook to promote the business of discounting bills and the method of payment by giro—that is, by means of transfers from one bank account to another—for which there was great need by reason of the quantity of copper money that was in circulation. For this purpose it established a dual institution which became known as the Copper Bank. It was intended that this bank should develop the giro system of payments, take interest-bearing deposits, and grant loans. It was founded mainly, however, for the purpose of “drawing silver money to the imperial money offices, and in particular to St. Petersburg.” This bank likewise failed to achieve any noteworthy results. The establishment of state banks of issue, begun in 1762, introduced a considerable advance in the matter of the granting of credit. The first attempt was a failure, but in 1768 two establishments were founded under the name of Assignation Bank. They were to facilitate monetary intercourse and to grant credit to private individuals. They were authorized to issue notes up to the sum of 1,000,000 rubles, for which they were to provide a cash cover consisting of copper money. Catharine II promised in her message that these notes would be forever redeemable and would never be appropriated by the Government (or lent to it) for its own purposes. This promise was not kept, and the volume of the notes (assignations) in circulation was increased in 1774 to 20,000,000 rubles, and in 1786 to as much as 50,000,000

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rubles. In the latter year these two establishments were replaced by a single Assignation Bank and the note circulation was raised to 100,000,000 rubles. Part of this was handed over to the Government in the way of a non-interest-bearing loan (26,000,000 rubles out of the fresh issue of 50,000,000 rubles). The remainder was to serve for the operations of the bank and to be assigned to the newly established state mortgage institution, the so-called Loan Bank, which was to take the place of the banks for the nobles created in 1754. There were now three kinds of mortgage institutions—the Loan Bank, the provident societies (“colleges”) for the service of the general public (1775),<sup>a</sup> and the deposit and loan institutions operated by the boards of guardians at the two imperial residences (1772). Subsequently an “Aid Bank for the Nobility” was established (1797–1802).

The Assignation Bank discounted bills and granted loans on collateral. The resources at its command were, however, very limited. It was replaced in 1817 by the newly founded Imperial Bank of Commerce. This bank received from the Government as its capital the sum of 30,000,000 rubles (16,000,000 rubles of which was, however, soon taken back) and was authorized to take deposits, discount bills, and to grant credit on the security of merchandise. The Bank of Commerce was in existence until the foundation of the Imperial Bank, and its affairs were wound up, along with those of the above-mentioned

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<sup>a</sup>The credit business of these “colleges,” which were benevolent institutions, was based on their privilege of taking deposits from private individuals and on the obligation imposed on government officials of transferring to them in the way of deposits all sums placed in the hands of the officials for safe-keeping or otherwise disposable.

credit institutions in 1859. The business of these banks reached the following dimensions:

The total amount of deposits in the Loan Bank increased from 31,520,000 rubles in 1817 to 109,120,000 in 1835, and to 412,760,000 in 1857. The great bulk of these deposits came from the Bank of Commerce, the "colleges" (provident societies mentioned above), and the officers of the Government. The deposits of private individuals amounted to about 15 per cent of the total. The loans in 1857 amounted to 368,300,000 rubles.

The deposit and loan institutions operated by the boards of guardians had deposits in 1859 aggregating 478,340,000 rubles, in addition to their capital aggregating 65,610,000 rubles, and the aggregate of their loans was 508,280,000 rubles.

The Bank of Commerce had deposits in 1856 aggregating 241,120,000 rubles, of which 222,020,000 rubles was deposited with the Loan Bank. In 1859 the aggregate of bills discounted reached the sum of 47,630,000 rubles.

The "colleges" (provident societies for the service of the general public) had deposits in 1858 aggregating 113,090,000 rubles. The aggregate of loans in that year was 128,710,000 rubles.

The above institutions had between them at the beginning of 1858 deposits aggregating 1,012,870,000 rubles and the aggregate of discounts and loans was 1,037,850,000 rubles.

It will be perceived that the main resources of these banks consisted of deposits withdrawable on demand. As against these liabilities there were long-term credits granted to landowners and the Government, the aggre-

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gate of whose obligations amounted on January 1, 1858, to 521,400,000 rubles. Only a small part of the resources of the banks was applied to the discounting of bills and to loans on merchandise. It was realized at an early date that such a condition was untenable, and in 1822 the minister of finance proposed the liquidation of the Loan Bank. This suggestion did not meet with favor and the plan was adopted of developing the institution further by concentrating in it the deposits of all the state banks. In 1830 the situation of the state institutions became still more precarious. At the suggestion of Count Kankrin the short-term obligations of the Government were converted into a long-term loan, bearing interest at the rate of 5 per cent, with an amortization of only 1 per cent, so that these funds were locked up for a period of thirty-seven years. The term of the new mortgage loans that were to be granted was lengthened considerably, and the rate of interest on deposits was reduced from 5 to 4 per cent. Thereupon there was an outflow of deposits from the state banks, which, by reason of the restricted field for the investment of capital, was followed by an inflow of money into the banks. A time came when the banks no longer found any opportunity for the profitable investment of the funds intrusted to them. In 1855 the sum of 20,000,000 rubles was lying idle, and at the middle of 1857 the amount reached 146,000,000 rubles. This situation could, in the nature of things, be nothing more than a transitory one, as new railways, joint-stock companies, and other undertakings had to place new issues of securities on the market. Instead of waiting for the natural outflow of the deposits or making greater efforts for their profitable utilization,

the administration of finance undertook a portentous reform. The ukase of July 20, 1857, decreed the lowering of the rate of interest on private deposits from 4 to 3 per cent, converted the thirty-seven-year debt of the Government into a fifty-six-year debt by fixing the yearly payment, including amortization, at  $4\frac{1}{2}$  per cent, and likewise ordered the yearly payments in the case of mortgages to be reduced. It was assumed that the anticipated withdrawals of deposits would ensue gradually, and that the banks, following the instructions of the finance minister, would be able to meet their obligations. It turned out very differently, however. The economic standstill of the days of the Kankrin régime was over. The money market offered capitalists all kinds of investments in the shape of government loans bearing a high rate of interest, stocks, bonds, etc. With the many new undertakings following one upon another, there was a veritable scramble for capital. In particular, the founders of the "Chief Association of Russian Railways" exerted their influence with the Government in the direction of lowering the rate of interest on deposits in order to set money free for the purposes of their undertakings. Deposits were consequently withdrawn in large sums and before long the administration of the banks had to face a crisis. The repayment of the deposits had to go on while it was not possible to realize on the assets. The ministry of finance sought to avert a crisis by prohibiting the establishment of new joint-stock companies, suspending loans on the estates of the nobles, and taking energetic steps to collect sums due. But these measures proved unavailing; nor could the imperial treasury lend any effectual aid. The ministry of finance

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then proceeded to fund the bank debt by means of two foreign loans, an issue of 4 per cent "inscription certificates," for which the 3 per cent deposit certificates might be exchanged, and another of 5 per cent bank notes. At the same time the liquidation of the state banks was decreed, the taking of deposits by the institutions was prohibited except in the case of the Bank of Commerce, and the deposit banks operated by the boards of guardians and the "colleges" (provident societies) were placed under the ministry of finance. In this way the reform of the state banking system was made to pass through a crisis by means of regulative measures requiring a vast outlay of money (over 1,000,000,000 rubles), an expenditure which without doubt delayed for a long time the reform of the monetary standard.

In 1860 the state banks were replaced by the newly established Imperial Bank. Private banking now developed vigorously, and Russia soon had modern private banks. The decade 1880-1890 witnessed again the creation of two state agricultural banks—the Peasants' Bank and the Bank for the Nobility. In 1894 the Imperial Bank was reconstituted and the reform of the monetary standard in 1896 marked for the institution the beginning of a period of far-reaching activity.

The history of banking in Russia presents the following characteristic features: The dominant rôle played by the state banking system and the consequent close connection between the banks and the national credit; the late beginnings of private banking and the complete absence of private banks of issue; the tendency toward a comprehensive regulation of private banking by the State.

## II.—THE EARLY ACTIVITIES OF THE IMPERIAL BANK.

The liquidation of the state credit institutions was assigned to the newly founded Imperial Bank (established May, 1860). The settlement with the depositors in the Loan Bank, the institutions operated by the boards of guardians, and the banks of the provident societies ("colleges") required extensive means, and, as the funds thus expended were only gradually restored to the bank, considerable sums of money were tied up for a long period. The sums expended by the bank for the purposes of liquidation were as follows:

	Rubles.
1860-1864-----	402, 079, 000
1865-1869-----	631, 545, 000
1870-1874-----	724, 824, 000
1875-1879-----	528, 756, 000
1880-1884-----	323, 487, 000
1885-1886-----	80, 489, 000

These operations crippled the bank in its legitimate activities, which should have been directed toward the promotion of business and the placing of the currency on a more solid basis. In 1886 it was relieved from the duties pertaining to the liquidation, but it had still to assist the state mortgage institutions with large sums of money.

The original capital of the Imperial Bank was 15,000,000 rubles and the surplus 1,000,000 rubles. The figures were raised by additions from the net profits to 25,000,000 and 3,000,000 rubles, respectively. The bank was authorized to receive deposits, but the right of issue was, as heretofore, to appertain to the Government.<sup>a</sup> The Imperial Bank was permitted to engage in the following kinds

<sup>a</sup> The resources of the bank consisted therefore almost exclusively of the deposits of private individuals.

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of business: The discounting of bills and other kinds of maturing paper; the loaning of money on collateral (securities, merchandise, precious metals); the taking of deposits; the purchase and sale of all kinds of securities on commission or for the account of the institution itself (the aggregate investment in the latter case being restricted to the amount of the capital). The bank was to be a purely state institution, placed directly under the minister of finance. It was provided that representatives of the nobility and the merchant class should have a share in the management. The operations of the institution were centralized and only a few branches were established. The interests of trade received but scant consideration, and the discounting of bills was hampered by red tape. It was not until 1892 that a better policy was inaugurated in the matter of discounts. In 1884 the Imperial Bank engaged in a new business, the loaning of money on mortgage to agriculturists. In 1892 various concessions were made to the agriculturists, and in particular to the nobles. Credits were to be granted for a term of from nine to twelve months, with the privilege of extension. The sums expended in such loans between 1884 and 1894 amounted to 99,000,000 rubles. By order of the Crown the bank also granted credit for other purposes, especially industrial undertakings. As originally constituted, the Imperial Bank did nothing toward the rehabilitation of the monetary standard.

In 1894 new statutes were framed for the Imperial Bank, and in 1896 the reform of the monetary standard was undertaken.

## III.—THE MUNICIPAL BANKS.

Such banks came into existence in 1789; but for some time they did not meet with great favor, so that down to 1862 no more than ten of them had been established. In that year the Government published "normal statutes for municipal banks," which facilitated the creation of new banks. As many as 215 such institutions were established between 1862 and 1883. A law was promulgated in 1883 aiming to protect the banks against mismanagement on the part of their officials and undue interference on the part of the city authorities and also to prevent the institutions from engaging in unprofitable business. The provisions of this law, in particular the more rigorous supervision exercised, hindered the multiplication of these banks. The increase in their number between 1883 and 1907 was only 39.

The establishment of such institutions is effected pursuant to the act of 1883 with the sanction of the Government (the minister of finance in accord with the minister of the interior). The original capital must amount to at least 10,000 rubles. The bank is under the supervision of the municipal assembly, to which it is accountable. The municipal assembly elects the board of directors of the bank. The directors are not permitted to fill any office in the municipal government or in any other credit institution. No one who is a member of the municipal assembly is eligible as a director, neither is any relative of a member of the municipal council. Two persons who are relatives or who are members of one and the same business house may not serve simultaneously on the board of directors. A special committee, with the president of the

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bank at its head, composed of delegates specially chosen for the purpose, may be organized to arrange matters pertaining to discount. The above-mentioned restrictions apply to the choice of these delegates also. By means of these restrictions the banks and their customers are to be guarded against undue exercise of authority on the part of the municipal government. The annual statements are presented to the municipal assembly, which chooses a revisory committee for the purpose of verifying them. The cash account is overhauled every month by the mayor and two members of the municipal council and has to be submitted for examination at any time at the request of the municipal assembly. After being examined, the report is sent in, together with the written opinion of the committee and the resolutions of the municipal council, to the finance minister and the minister of the interior. The Government may institute an examination either on the application of the governor of the province, based on the request of the municipal assembly or of a portion of its members, or at the instance of the finance minister, acting in accord with the minister of the interior. In addition to this, the banks are required to furnish every kind of information regarding their affairs to the ministry of finance. The minister of finance is authorized to prescribe the formularies to be employed in the balance sheets and regulations relative to the business of the banks.

The banks may engage in the following kinds of transactions:

The taking of deposits; the discounting of bills; the loaning of money on collateral (securities, merchandise, and also real estate), and the opening of accounts current

on the deposit, as security, of government obligations or obligations guaranteed by the Government or of warehouse certificates (deposits of grain); the collection of bills and other maturing paper for account of third parties; the transfer of sums of money (only if the amount has been actually paid in) to any place where the bank has a correspondent; the purchase and sale of all kinds of securities for account of other parties; the purchase and sale of government obligations and obligations guaranteed by the Government for account of the institution itself; the purchase and sale of the precious metals (coin and bullion) for account of other parties or of the bank; the pledging of the securities belonging to the bank to other banking institutions; the pledging of the securities placed in the hands of the bank as collateral to other banking institutions, this to be done only with the consent of the owner.

The aggregate of the liabilities of the bank shall not exceed five times the amount of its capital. The amount of the credit granted to any single individual in any shape or form shall not exceed one-tenth of the capital. The directors and employees, as well as the mayor and the members of the municipal council, can obtain credit only subject to various restrictions. The cash reserve, together with the credit balance at the Imperial Bank, shall not be allowed to sink below 10 per cent of the total liabilities. An important feature of these institutions is the fact that the security afforded the depositors lies not merely in the capital of the bank, but also in the mortgage of some part (a definite item) of the city's property. In the withdrawal of deposits payable on demand previous notice is required, the time ranging from one week to three months.

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Real estate on which money is loaned on mortgage must consist of parcels of ground or buildings located in the same city or of estates located in the same government. The city real estate may be dwellings, warehouses and stores, factories, workshops, or other buildings. Mortgage loans in connection with real estate that yields no income are prohibited. In the case of buildings the time within which the sum loaned on mortgage is to be repaid varies from one year to eight years. In the case of landed estates the term may extend to as much as twelve years. Loans granted for as long a term as eight years are not to be repaid at a single payment. In the case of an eight-year term, after the expiration of three years one-fifth of the amount is to be repaid annually until the indebtedness is extinguished, and in the case of a twelve-year term, after the expiration of two years one-tenth of the amount of the loan is to be repaid annually. The amount of the mortgage is not to exceed one-half of the value of the property.

A percentage of the net profits, varying from 10 to 20 per cent, is to go to the surplus, until the surplus reaches the sum provided for in the statutes of the bank. The surplus is intended to cover losses that may be incurred by the bank, and is either to be deposited in the Imperial Bank or invested in government bonds. The remainder of the profits may be devoted to municipal or to benevolent purposes. The city may, with the sanction of the Government, secure a loan at the bank, the sum to be taken from the original capital. Unexpended profits go to increasing the capital.

## IV.—CREDIT ASSOCIATIONS BASED ON MUTUAL HELP.

These are associations with limited liability, whose capital is created by the imbursements of members, fixed at one-tenth of the amount of the credit granted them. The maximum imbursement of any one member shall not be in excess of fifty times the amount of the smallest imbursement. The obligation to make after-payments is limited by the amount of the credit granted. It is not lawful to belong to more than one of these credit associations. Business is to be done with members only. Exceptionally, however, credit may be granted, with the sanction of the finance minister, to rural communes and peasants' associations. The governing body is the general assembly. If this is very numerous, it may be replaced by an executive council. Associations of this kind may also be established as self-governing corporations by the zemstvos of the governments and the smaller administrative divisions, called "circles."

The first of these credit associations was established at St. Petersburg in 1862 after the pattern of the "Union du crédit" of Brussels. By the year 1883 there were 87 of them. From 1883 to 1893 the creation of such institutions was interdicted. Between 1894 and 1908 as many as 232 new ones were established. A project has been on foot the last few years for the establishment of a central bank for credit associations, as they can not obtain sufficient credit either at the Imperial Bank or at the private banks.

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## V.—PRIVATE BANKS.

After the liquidation of the state credit institutions the Government permitted the establishment of private banks, which previously—to quote the words of the minister of finance, Count Kankrin—were regarded “as extremely dangerous institutions that ought not to be tolerated at all.” The first joint-stock bank (the Private Bank of Commerce of St. Petersburg) was established in 1864 with the assistance of the Government, which subscribed to one-fifth of the stock. Between 1864 and 1874 no fewer than 39 private banks were founded. This feverish activity, however, on the part of promoters was suppressed by the act of May 31, 1872, which interdicted for the time being the establishment of new joint-stock banks in the two imperial residences (St. Petersburg and Moscow) or any city in which a private bank already existed. After an interval of some years, ending in 1879, new banks made their appearance, 12 of them being established between that date and 1908. At present there are 36 joint-stock banks.<sup>a</sup> Since 1891 the Crédit Lyonnais has had a branch at St. Petersburg.

The establishment of joint-stock banks is effected in accordance with the provisions of the law of 1883. In cases where deviations from these regulations are deemed

<sup>a</sup> The largest banks, with the amount of their business, as given to the public in the annual statement published at the beginning of 1907, are: The Volga-Kama Bank, 199,000,000 rubles; the Russian Bank for Foreign Trade, 198,000,000 rubles; the St. Petersburg International Bank, 193,000,000 rubles; the Azov-Don Bank, 151,000,000 rubles; the Moscow Bank of Commerce, 147,000,000 rubles; the Northern Bank, 144,000,000 rubles; the St. Petersburg Discount Bank, 97,000,000 rubles; the Russian Bank for Trade and Industry, 84,000,000 rubles; the Siberian Bank, 62,000,000 rubles.

desirable the minister of finance has to submit a bill relative to the matter to the national assembly. According to the provisions in force at present, the original capital of the bank is not to exceed 5,000,000 rubles. One-half of this capital is to be paid in at the time the shares are subscribed for and the remainder within six months. The liabilities are not permitted to be in excess of five times the amount of the bank's capital. The bank is obliged to keep at least one-tenth of the total amount of its liabilities in cash or in the form of a credit balance at the Imperial Bank. The maximum credit granted to any one customer shall not exceed one-tenth of the original capital of the bank, and the same restriction applies to the aggregate of blank credits. The bank is allowed to issue only certificates of deposit, the negotiation of which must be recorded by an entry in the books of the bank. The banks are obliged to create a surplus fund, one-half of the net profits above 10 per cent being taken for the purpose. The general assembly of the shareholders may resolve that part of the surplus may be used for increasing the dividend in case this falls short of 8 per cent. Two-thirds of the surplus fund may be invested by the bank, but one-third has to be deposited in the Imperial Bank in the shape of government bonds or securities guaranteed by the Government. The members of the board of managers (with the exception of the advisory members), as well as the president and the officials, are not to obtain credit at the bank in any shape or form. No person is allowed to be a member of the board of managers (or of the advisory board) of more than one bank. The rights of the minority are secured by the provision that no

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shareholder shall, at a general meeting of the shareholders, have a voting power exceeding one-tenth of the aggregate number of votes of the members present. An examination of the affairs of the bank by the ministry of finance is made not merely in pursuance of a resolution of the general assembly of the stockholders, but also on the application of a minority if it commands one-tenth of the aggregate number of votes at a general meeting of the shareholders and represents one-twentieth of the capital. Such minority may apply for an examination at the hands of the finance minister independently of the general assembly.

A word remains to be said concerning banking and bill-brokerage houses. Private banking concerns which are not incorporated are under the supervision of the finance minister, who may at any time ask for information regarding their business and send examiners to overhaul their accounts. In case the examination reveals any abuses, the minister is authorized to prohibit certain kinds of business, as, for instance, the taking of deposits. The ministry of finance has recently been contemplating a very thoroughgoing regulation of private banking. Above all, the kinds of business in which the individual concerns are allowed to engage are to be distinctly defined and regulated by legal prescription, and banking houses that receive deposits are to be obliged to publish periodical statements.

VI.—THE NEW STATUTES OF THE IMPERIAL BANK.

The main provisions of the new statutes of the Imperial Bank, which received the imperial sanction on June 18, 1894, are as follows:

The capital of the bank (hitherto 25,000,000 rubles) may be increased to 50,000,000 rubles and the surplus (hitherto 3,000,000 rubles) to 5,000,000 rubles. Until this limit is reached (apart from possible accessions not provided for) 10 per cent of the annual profits are to go to the enlargement of the capital and 5 per cent to the surplus. Any deficit that the bank may sustain is to be covered by the surplus, and in case the surplus is exhausted the amount is to be charged to the imperial treasury, which, on the other hand, is to be credited with the amount of the net profit remaining after the above-mentioned percentages have been assigned to the bank and after deduction of bonuses and pensions to employees. The bank is under the direct control of the minister of finance, who is at the head of the management. The central administration consists of a council of the bank, a governor, and two deputy governors. The branch offices are divided into main branches and secondary branches. Each office has a committee for discounts and loans, which has to pass on the security of the paper handed in and the value of the collateral and to determine the maximum credit to be granted in the case of each customer.

The business of the bank comprises the discounting of bills and other paper maturing at a fixed date, the granting of loans and credits, the taking of deposits and the reception of valuables for safekeeping, the purchase and sale of bills and other paper, the issue

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of drafts drawn in one locality upon some other place, and buying and selling on commission. There are special provisions relative to the various kinds of transactions, some of which are noteworthy. The paper discounted by the bank may be either bills or promissory notes, which may originate abroad as well as at home. They have to be made payable at a banking town, must bear at least two good signatures, and must mature within six months (in the case of some regions, twelve months). The bank is allowed to take notes not resting on a consummated commercial transaction but put forth with reference to the prospective needs of some mercantile or industrial undertaking. The rate of discount has to be fixed at least once every quarter of a year, and it may vary in the case of different kinds of business and different localities. The minister of finance may exceptionally grant an extension in the case of protested or nonprotested bills or leave to pay in installments, but only if a mortgage or other pledge deemed sufficient by the council of the bank is offered as security.

The bank grants so-called industrial loans against promissory notes bearing merely the signature of the debtor, such notes being secured either by mortgages on real estate, by mortgages on the appurtenances of farmed lands or of industrial plants, by the guaranty of third parties, or by some other collateral which the minister of finance deems sufficient. When the amount of the loan does not exceed 300 rubles the managers of the branch office concerned may resolve to grant the credit even without such special security. The industrial credit must be intended for some specific purpose indicated by the person applying for the credit and can

only be granted in order to afford the borrower working capital or to enable the agriculturist or manufacturer to provide the necessary outfit for his farm or factory, or in order to afford similar assistance to the artisan, the retail merchant, or to the worker in some house industry. The machines and implements that serve as security must be of Russian manufacture. Exceptions may be made in certain cases by the finance minister, or conjointly by him and the minister of agriculture. The amount of credit allowed in the case of any individual industrial undertaking is not to exceed 500,000 rubles, and in the case of the owners of small workshops the maximum amount is 600 rubles. Loans for the purpose of procuring machinery, implements, etc., shall not run for more than three years. When the time of the loan exceeds six months, provision must be made for the repayment in regular installments. Loans shall not exceed 50 per cent of the appraised value of the articles mortgaged. Those loans which are granted for the purpose of providing working capital are not to exceed 75 per cent of the amount required in the way of such capital. The borrower must bind himself by a special document to use the money only for the particular purpose indicated and to keep up the articles that serve as security to their full value. In the case of loans of this kind the bank is authorized by paragraph 8 of the regulations to permit (with certain precautions) the articles mortgaged to remain in the hands or in the safe-keeping of the borrower.

The bank grants, moreover, credit on nonperishable wares of Russian manufacture, warehouse certificates, bills of lading, etc. Loans on foreign goods may be granted only

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pursuant to a resolution of the council of the bank, confirmed by the minister of finance. Loans on merchandise and warehouse certificates are not to run over nine months, those on bills of lading not over three months, and those on metals not over fifteen months. Extensions of time in the repayment of loans on merchandise shall not exceed three months. Loans on merchandise shall not exceed two-thirds of the value as appraised by the committee on loans. In the case of warehouse certificates and railway bills of lading (the loans on the latter being for six weeks) the maximum is 80 per cent. If the goods offered as security depreciate in value or fall in price to the extent of 15 per cent below the appraisal, the debtor must on request of the bank repay a corresponding fraction of the loan or else put up additional security. If, however, the price has fallen as a result of unusual circumstances, the council of the bank is permitted to grant an extension or to release the borrower from the necessity of making a partial repayment or of putting up additional security. Persons enjoying the implicit confidence of the bank may be granted credit on the security of goods other than those contained in the list prepared by the council of the bank. The security may, furthermore, be left in the possession of the borrower, and the amount loaned may run as high as 75 per cent of the value of the security.

The bank grants six months' loans on government securities and securities guaranteed by the Government up to 90 per cent of their value. In the case of mortgage debentures the ratio is 80 per cent and in the case of other securities allowed by the council of the bank it is 75 per cent. The term for which the loan may be renewed shall not exceed three months. Special accounts current are

opened against the deposit of securities, the depositor being permitted to draw up to a certain sum, paying interest only on the amount that he owes to the bank. The bank may also, as far as it has any available resources left, grant credit to the governments (main administrative divisions), circles (districts), and cities. It may, in addition, by means of intermediaries, grant credit to small agriculturists, peasants, leaseholders, and artisans on the security of the products of their industry, and it may also advance money for the purchase of machinery, implements, or other equipment, or the creation of a working capital. It may likewise make advances on merchandise in transit or about to be shipped. The intermediaries may be the provincial or district assemblies, the credit institutions, loan associations, or the artels (associations of workingmen) in so far as their statutes have received the sanction of the Government and they are willing to subject themselves to the prescribed conditions and the supervision of the bank. Private individuals also, residing in the same place as the borrower, in whom the bank has confidence, may be made use of as intermediaries. In the case of goods in transit the intermediaries are the railways and transportation companies. The intermediaries assume full responsibility for the sums advanced to them by the bank. The zemstvos (government and district assemblies) may, however, with the sanction of the minister of finance, limit their liability to the preservation or maintenance of the goods assigned as security.

The bank takes both deposits repayable on demand and deposits repayable only at the expiration of a certain time. The conditions relative to the taking of deposits

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are fixed by the council of the bank with the sanction of the finance minister, and any changes must be announced a month in advance.<sup>a</sup> The depositors dispose of their credit balance by means of checks and drafts.

No other state institution has hitherto attempted to grant credit to agriculturists and manufacturers so readily and with the exercise of such leniency in the event of difficulty of repayment. In addition to the kinds of loans authorized by the statutes of the bank, long-term loans have been granted "by virtue of special provisions" up to large sums (even 6,000,000 to 9,000,000 rubles) for various purposes, as the support of banks, industrial undertakings, a hotel company, etc., and in aid of such undertakings as mines, harbor improvements, etc. There is no special account of such loans figuring in the statements of the Imperial Bank. According to the report of the imperial comptroller of finances, the aggregate amount in 1900 was about 41,000,000 rubles, 65,000,000 in 1901, and over 100,000,000 in 1902. After the last-mentioned date the granting of loans of this kind was greatly restricted, although they were not discontinued. At the beginning of 1905 the aggregate was 72,600,000 rubles and at the beginning of 1906 it was 72,000,000 rubles. To this latter amount must be added, in the opinion of the comptroller, the sum of 58,400,000 rubles, representing various kinds of transactions not

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<sup>a</sup> From 1860 to 1886 interest was allowed on account-current deposits up to 3 per cent (from 1875 only 2 per cent in St. Petersburg and Moscow, and in the case of the deposits of private banks only 1 per cent); from 1886 to 1889 the maximum rate was 1 per cent; from 1889 to 1906 no interest was allowed; from 1906 to May 1, 1908, the maximum rate was 2 per cent; since the last-mentioned date such deposits pay no interest.

enumerated in the statutes of the bank. Loans granted "by virtue of special provisions" (that is to say, in pursuance of imperial orders) have occasioned great losses. Down to the beginning of 1906 a total of 25,600,000 rubles had been paid out of the net profits of the bank in order to cover doubtful debts. Such loans are altogether improper, and even loans for industrial purposes, granted in accordance with the statutes of the bank, ought to be made with due caution and only up to a certain aggregate amount. Now that the bank is bound to make specie payments and has to provide for the perpetual redemption of its notes, it is all the more incumbent upon it to be careful not to tie up its resources in investments not suited to a bank of issue.

#### VII.—THE RESUMPTION OF SPECIE PAYMENTS.

The resumption of specie payments by the Imperial Bank on the basis of the gold standard has been successfully accomplished after several years' preparation through the energy of the finance minister, Witte, in the face of strong opposition on the part of large sections of the public.

The first thing to be attained was the reduction of the volume of notes in circulation and the enlargement of the stock of gold in the bank and in the imperial treasury. The issue of notes had previously been something apart from the mercantile business of the bank, so that it might almost have been said that there existed, as in the case of the Bank of England, an issue department and a banking department. In the course of the Russo-Turkish war of 1877-78, however, credit bills up to an aggregate

amount of 417,000,000 rubles had been "temporarily" issued for account of the banking department, of which 266,263,146 rubles were outstanding in 1891. This temporary issue was secured by government bonds up to the sum of 173,500,000 rubles and by loans to private customers for the remainder. By the ukase of July 28, 1891, a temporary note issue of 75,000,000 rubles was made for the issue department, and simultaneously the redemption fund was increased by an equal nominal amount in gold rubles taken from the resources of the bank and the gold in the imperial treasury. The reserve was thereby raised to 285,379,000 rubles in gold (nominal value) and 1,126,000 rubles in silver, against which there was at that time a fixed note issue of 780,032,000 rubles and the new temporary issue of 75,000,000 rubles. The ukase of December 9, 1894, provided that the 266,263,146 rubles which figured as a temporary expenditure in the liabilities of the mercantile department be transferred to the issue department and be permanently kept in circulation. The 5 per cent government bonds assigned as a partial cover were to be canceled, and for the remainder of the cover (92,734,591 rubles) an equivalent sum in gold, according to the existing premium (65,433,691 rubles), was to be assigned to the issue department. In this way the amount of gold in the issue department was raised to 350,813,041 rubles (nominal value), there being a fixed circulation of 1,046,282,000 rubles and a temporary issue of 75,000,000 rubles. By the ukase of March 15, 1895, an additional 98,061,276 rubles in gold was transferred from the imperial treasury to the reserve of the issue department, which was thus raised to

375,000,000 rubles as a cover for the fixed circulation or altogether to 450,000,000 rubles, reckoning the cover for the temporary 75,000,000 rubles (the 1,125,082 rubles in silver having been replaced by an equivalent amount of gold).

There was a further accession of 50,000,000 rubles in gold to the metallic reserve constituting the redemption fund at the beginning of 1896, and, in addition, the ukase of February 23 of that year decreed that one-half of the 75,000,000 rubles which had been set aside as a cover for the temporary issue of 1891 be assigned to the reserve, while at the same time the authorized note circulation was reduced by 52,500,000 rubles (paper), that is to say, from 1,121,300,000 rubles to 1,068,800,000 rubles. The reserve was thus increased to 462,500,000 gold rubles (old rubles). In the meanwhile, in December, 1895, the half imperial (5 rubles) had been declared equivalent to 7½ paper rubles and this ratio was definitely established for the time being by the ukase of August 8 (new style, August 20), 1896. The Imperial Bank was now ready to pay out gold on demand in exchange for paper at this ratio. The ukase of January 3 (15), 1897, introduced a new gold monetary unit, the gold coins of the weight and fineness of imperials and half imperials being now stamped with the imprint of 15 rubles and 7½ rubles, respectively. At the same time the Imperial Bank announced that it would buy, sell, and accept in payment gold coins at the established valence. The resumption of specie payments was thus practically consummated. That this reform was so splendidly accomplished in Russia, while in Austria, for example, it could still not be effected, was due

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primarily to the collecting of an immense stock of gold. According to information furnished by Prof. H. von Kauffmann, of St. Petersburg (one of the directors of the bank), the gold reserve of the Imperial Bank, inclusive of credit balances (gold) abroad, foreign bills payable in gold, and the gold deposited by the imperial treasury for safe-keeping in the bank, was as follows at successive dates, the imperial being reckoned at 15 rubles (the ruble being equivalent to 2.16 marks):

Beginning of—	Rubles.
1884	297, 630, 000
1887	381, 940, 000
1890	475, 190, 000
1893	851, 740, 000
1896	963, 780, 000
September 8, 1897	1, 144, 880, 000

The increase from 1884 was therefore no less than 847,250,000 new rubles or 2,259,000,000 francs. The stock in September, 1897, was equivalent to 3,053,000,000 francs, which was the largest supply of gold that had ever been collected at one place.

This colossal sum of 1,144,880,000 rubles, according to the classification existing on September 8 (20), 1897, before the ukase of August 29 (September 10), 1897, went into force, was divided up as follows:

1. Reserve of the issue department, 462,500,000 rubles (old rubles) gold.
2. Cover for the temporary note issue of 1891 (being one-half of the amount of the issue), 37,500,000 rubles gold.
3. Gold belonging to the imperial treasury, deposited in the bank, consisting of the sum of 75,000,000 rubles, intended, in pursuance of the ukase of July 8, 1896, for

the diminution of the debt of the state incurred for notes issued and of 75,045,754 rubles other gold. This gold of the imperial treasury, equivalent to 225,070,000 new rubles, figured as a special item in the publication of the bank's balance sheet down to August 29, 1897.

4. Gold coin in the cash of the mercantile department of the bank, 50,790,000 rubles (new rubles) gold.

5. Other gold in the possession of the mercantile department, 81,170,000 rubles.

6. Money in the mint belonging to the Government, 24,650,000 rubles (new rubles) gold.

7. Credit balances in foreign countries (gold), 13,120,000 rubles (credit balances directly belonging to the Government not being reckoned).

8. Foreign gold bills in the possession of the bank, 92,328 rubles.

There was in addition lying in the bank in connection with custom-house business, 83,345 rubles in gold coin.

#### VIII.—THE SITUATION AFTER 1897.

In pursuance of the ukase of August 29, 1897, the balance sheet of the bank has been drawn up in an entirely different way since September 8 (20), 1897. The account is made up exclusively in new rubles, and the 462,500,000 plus 37,500,000 (500,000,000) rubles (old rubles) gold, which figured previously as a reserve against the fixed issue and the temporary issue of notes, was now entered in the shape of 750,000,000 rubles. This sum is, however, no longer entered separately but in combination with the gold of the imperial treasury, which was formerly kept apart in the publication of the balance sheet (225,070,000

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new rubles on September 8, 1897). The new gold pieces, coined after March 1, 1897, are not included in the cash. The rest of the gold is entered in the form of various items. The balance sheet for September 8 (20), 1897, drawn up in accordance with the new provisions (relative to the central bank and to its branches) exhibits the following assets:

	Rubles.
Bank notes in the bank and at its branches, etc.....	57, 210, 000
Silver and copper coins.....	43, 030, 000
New gold coins.....	104, 490, 000
Old and foreign gold coins, bullion, and gold certificates.....	1, 027, 190, 000
Gold as a reserve against certificates of deposit.....	80, 000
Credit balances in foreign banks (gold).....	13, 120, 000
Foreign gold bills.....	90, 000
Uncovered debt of the Government on account of notes issued.....	206, 280, 000
Discounted bills, loans on collateral, and various sums due the bank.....	342, 280, 000

The principal items in the liabilities were:

	Rubles.
Notes in circulation.....	1, 068, 780, 000
Certificates of deposit in circulation.....	80, 000
Capital.....	53, 000, 000
Credit balance of the Government.....	239, 410, 000
Other deposits.....	405, 110, 000
Bills drawn by the bank on foreign countries.....	2, 040, 000

The uncovered obligations of the Government, which previously, when the note issue was 1,068,780,000 rubles, were reckoned at 568,780,000 rubles, are thus reduced in this statement to 206,280,000 rubles, the 500,000,000 old rubles (gold) of the reserve being now reckoned as 750,000,000 new rubles, and the 75,000,000 old rubles deposited by the imperial treasury in the bank in 1896 (as mentioned above) having been converted into 112,500,000 new rubles. The remainder of the gold belonging to the Government—the 75,050,000 old rubles,

and the 24,650,000 old rubles lying in the mint—was placed to its credit on current account, while being still included in the aggregate metallic reserve of the bank. Only the credit balances of the Government in foreign institutions, the amount of which was not made public, were thus left out in the bank statement.

In setting down the figure of the actual note circulation at the above-mentioned date, September 8 (20), 1897, it is necessary to deduct from the amount of the note issue the aggregate of the notes lying in the bank and at its branches and in the offices receiving and disbursing money for the Government, amounting to 57,210,000 rubles, which leaves the sum of 1,011,570,000 rubles.

The aggregate stock of gold in the bank on September 8 (20), 1897, was 76,000,000 rubles in excess of the authorized issue of notes and 132,000,000 rubles in excess of the actual circulation. Of course, this gold was also to serve as a reserve against the public and private deposits, but even after taking this into account the figure was not a poor one. It must be remembered that one-third of the total deposits represented the credit balance of the Government on current account, which was more than offset by the uncovered obligations of the Government.

The assurance of the redemption of the notes in the near future was thus provided for by the ukase of August 29 (September 10), 1897. The notes, secured by a gold reserve, were to be issued by the Imperial Bank in amounts strictly limited by the needs of the money market. The gold reserve against the issue must amount

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to one-half of the volume of notes issued up to an issue of 600,000,000 rubles, and any excess above 600,000,000 rubles must be covered by at least an equal amount of gold, ruble for ruble, every fifteen credit rubles being covered by one imperial.

This meant practically that the bank was authorized to issue notes up to 300,000,000 rubles without metallic cover. The bill originally drawn up for the reform of the currency fixed a larger amount, 500,000,000 rubles, providing that the issue up to 1,000,000,000 rubles was to be secured by a one-half gold reserve, and that any excess over that amount was to be fully covered.

The ukase of November 14 (26), 1897, decreed the coinage of gold five-ruble pieces according to the new monetary unit, and another ukase of the same date brought the reform to a formal termination by decreeing that the Imperial Bank was to redeem the notes in gold without any limitation, and that their redemption was guaranteed by the entire resources of the Government. The notes, as a matter of fact, continued to be a legal tender, bearing the imprint "national credit bill." A ukase of March 27 (April 8), 1898, fixed the maximum coinage of silver at 3 rubles per head of the population and limited the legal-tender quality of the full-weight silver coins to 25 rubles. The full-weight silver coins, of which the bank had 27,820,000 rubles on September 8 (20), 1897, and the subsidiary silver coins and copper coins, which together amounted to 15,210,000 rubles (the aggregate of these various kinds of currency in the possession of the bank being therefore 43,030,000 rubles), were—contrary to what obtained in the case of the

German Imperial Bank—not to be reckoned part of the reserve against circulation. The present Russian coinage system is based on the law of June 27 (July 9), 1899. The gold ruble is the monetary unit of the empire and is supposed to contain 0.774234 grams of pure gold (17,424 doli).

In the course of the year 1898 the condition of the Imperial Bank was still further improved. On the one hand the volume of outstanding notes, and on the other the uncovered debt of the Government to the bank, were diminished, the former being reduced from 1,019,000,000 to 901,000,000 rubles, and the latter cut down to 100,000,000 rubles. The diminution of the circulation was effected mainly by the calling in of the one-ruble and three-ruble notes, which were to be gradually replaced by silver coin. The obligations of the Government (note debts) were reduced in the twelve years 1887-1898 by 439,900,000 rubles, which reduction was accompanied by corresponding withdrawal of notes from circulation. But even the 100,000,000 rubles of uncovered obligations were regarded as an objectionable item. The ukase of December 4, 1899 (January 5, 1900), decreed that 50,000,000 rubles of this debt be paid out of the receipts of the Government for 1899, and the ukase of April 28 (May 11), 1900, assigned another 50,000,000 rubles from the imperial treasury to the bank. By this latter act the debt of the Government to the Imperial Bank was definitively extinguished. The liquidation of this debt was zealously advocated by Lexis and H. von Kauffmann.

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## IX.—THE IMPERIAL BANK AND THE CURRENCY IN RECENT YEARS.

A feature of the policy of the Imperial Bank, rendered necessary by considerations with respect to the redeemability of the notes, is the limited scale on which the business of granting loans of a kind not suitable for a bank of issue is carried on. The following figures will show how moderate the activity of the bank is in this direction:

Year.	Paid out in loans to manu- facturers.		Paid out in loans to agri- culturists.	
	Rubles.	Rubles.	Rubles.	Rubles.
1896	20,000,000		30,000,000	
1898	13,300,000		14,400,000	
1900	60,000,000		12,200,000	
1901	77,400,000		12,200,000	
1904	54,300,000		15,100,100	
1905	45,100,000		15,500,000	
1906	49,900,000		14,000,000	

It must be borne in mind, however, that the "industrial" loans are in large part placed to the account of advances on securities and bills (special accounts current) and not included in the above figures. Apart from loans granted "by virtue of special provisions," even the industrial loans sanctioned by the statutes of the bank are not a fit investment for a bank of issue, a fact especially brought out at a time of crisis. Least of all are such advances suitable for the Russian Imperial Bank, which is permitted to make nearly all its loans for terms ranging from six to nine and even twelve months, which makes it much more difficult for it to realize on its assets.

The question has been often asked recently whether the foreign "gold credit balances" of the Imperial Bank

can be regarded as a cover for note circulation. These balances are the sums payable on demand that the Imperial Bank has with foreign banks, which have to pay back these deposits in gold. They originate mainly through the assignment by the imperial treasury to the Imperial Bank of sums realized or to be realized from foreign loans, which sums the Imperial Bank has then placed to its credit abroad, handing over the equivalent in notes to the imperial treasury. This takes place in the case of the so-called "reports," when the Imperial Bank is the intermediary between the foreign lenders and the Russian borrowers. As far back as 1897 the council of the bank expressed its opinion to the effect that this foreign credit balance might be included in the reserve. This opinion was confirmed by the finance minister in conjunction with the imperial comptroller. There is no doubt, however, that the letter of the law does not admit of such an interpretation. That the Imperial Bank in the event of a run upon it will not be in a position to get hold of this gold balance and bring it over is evidenced by the fact that in 1905, when the visible gold reserve of the bank had dropped from 880,400,000 to 623,700,000 rubles, there was an export of gold amounting to 50,000,000 rubles. At that time the bank management took measures to retard the redemption of the notes in gold, restricted the sale of drafts on foreign places, and sought to induce the private banks to secure an extension of their credits abroad, so as to check the drain of gold from the Imperial Bank. The amount of gold in circulation in the country decreased in the course of the year 1906 from 837,800,000 to 641,900,000 rubles, while the volume of notes in circulation remained about

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the same—1,207,500,000 rubles at the close of 1905 and 1,194,600,000 rubles at the close of 1906. This ought to make it evident that the foreign gold can not be an actual reserve against notes. Official journals have pointed to the fact that other banks of issue include foreign bills in their reserve. The managers of the Imperial Bank appear to be of opinion, however, that credit balances abroad can not be placed on a level with drafts, of which a separate account is kept.<sup>a</sup>

The foreign "gold" ought not to be reckoned part of the reserve of the Imperial Bank. If a larger circulation

<sup>a</sup> The foreign bills in the portfolio of the bank may properly be regarded as a reserve against notes, as it is possible to realize on them at any moment in the domestic market, the direct result of which is either the immediate strengthening of the gold reserve of the bank or the contraction of the volume of notes in circulation. But the bank could dispose of its foreign credit balances only in a limited measure by reason of the needs of its foreign financial business. The subjoined table gives the aggregate of foreign credit balances and the amount of foreign bills for the ten years 1899–1908, together with the amount of gold in the vaults of the bank, the movement of gold in and out of the country, and the volume of notes in circulation. It will be seen that there is no relation between the total of foreign gold credits and the amount of foreign bills. The figures are in millions of rubles.

Beginning of the year—	Amount of gold in the vaults of the bank.	Foreign credit balances.	Foreign bills.	Movement of gold.		Notes in circulation.
				Imports.	Exports.	
1899-----	991.1	16.1	0.005	-----	14.6	661.8
1900-----	833.4	6.1	3.5	-----	122.5	491.1
1901-----	708.2	24.7	2.8	-----	67.7	555.0
1902-----	682.2	26.6	0.7	19.3	-----	542.4
1903-----	708.5	58.2	2.5	21.9	-----	553.8
1904-----	734.0	167.0	8.1	-----	0.2	578.4
1905-----	880.4	146.9	4.3	-----	50.0	853.7
1906-----	717.0	208.8	0.7	-----	60.7	1,207.5
1907-----	889.9	298.5	2.2	-----	-----	1,194.6
1908-----	944.4	213.1	4.0	-----	-----	1,155.1

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of notes is desirable, there is nothing to be done but to amend the law. If an uncovered circulation of 300,000,000 rubles should be deemed sufficient, then every ruble in circulation in excess of that amount has to be secured by gold in the vaults of the bank.

There has been an agitation recently in behalf of a reformation of the Imperial Bank, which it is proposed to convert into an autonomous institution, independent of the minister of finance.

Schmoller remarks justly ("Grundriss" II, 221) that "the great banks that formerly existed in Russia, as well as the Russian Imperial Bank, were and are merely subsidiary organs of the ministry of finance." It would be a good thing if the statements of the bank were submitted to the Imperial Duma for inspection. According to the legal provisions now in force, they are examined by the second department of the council of state in closed session.

## X.—STATISTICS OF RUSSIAN BANKING INSTITUTIONS.

### THE IMPERIAL BANK FROM 1898 TO 1908.

[Main items in the balance sheet in millions of rubles.]

Beginning of the year—	Gold, in- clusive of credit balances abroad and for- eign bills.	Notes in circula- tion.	De- posits.	Dis- counts and spe- cial ac- counts current (credit against bills).	Loans on—		Advances to—	
					Securi- ties.	Mer- chan- dise.	Agri- cultur- ists.	Manu- factur- ers.
1898-----	1,169.3	901.0	665.2	155.1	62.7	22.9	14.7	11.0
1899-----	1,008.0	661.8	665.0	167.9	52.2	22.2	9.6	8.7
1900-----	843.0	491.1	789.7	245.3	73.0	29.4	8.4	22.5
1901-----	737.4	555.0	649.1	267.0	107.7	42.2	8.0	38.8
1902-----	709.4	542.4	709.0	279.5	127.4	46.8	7.4	38.2
1903-----	769.2	553.8	678.1	263.8	110.7	46.0	7.6	39.2
1904-----	909.1	578.4	808.5	267.5	100.1	52.4	8.0	36.0
1905-----	1,031.6	853.7	608.7	182.6	110.6	51.3	8.4	35.8
1906-----	919.7	1,207.5	529.2	359.4	281.4	66.4	9.8	27.8
1907-----	1,190.3	1,194.6	566.9	232.8	170.0	58.4	9.2	31.1
1908-----	1,161.5	1,155.1	606.8	281.9	152.8	63.3	9.8	32.8

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## JOINT-STOCK BANKS.

[In millions of rubles.]

Beginning of the year—	Capital.	Deposits.	Securities.	Discounts and loans.
1898.....	235.3	468.0	91.6	636.7
1901.....	267.0	560.1	108.0	779.6
1904.....	266.4	747.6	112.4	1,011.1
1907.....	282.9	785.9	106.7	996.2

## MUNICIPAL BANKS.

[In millions of rubles.]

Beginning of the year—	Capital.	De- posits.	Securities.	Discounts and loans.	Mort- gages.
1898.....	36.7	89.1	10.8	75.5	26.4
1901.....	40.2	97.3	13.8	82.7	33.3
1904.....	43.9	106.8	15.1	84.7	42.0
1907.....	46.7	108.9	14.8	83.8	47.0

## CREDIT ASSOCIATIONS BASED ON MUTUAL HELP.

[In millions of rubles.]

Beginning of the year—	Capital and sur- plus.	Deposits.	Securities.	Discounts and loans.
1898.....	29.8	143.8	6.1	168.4
1901.....	37.6	178.1	9.9	222.5
1904.....	43.2	214.1	15.9	239.9
1907.....	47.3	202.9	15.8	245.5



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# The Bank of The Netherlands

BY

R. VAN DER BORGH

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[From Conrad's *Handwörterbuch der Staatswissenschaften*, 3d edition]

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## THE BANK OF THE NETHERLANDS.

The central bank of issue of the Netherlands, the Bank of the Netherlands—a joint-stock company—was created by the royal decree of March 25, 1814. Its charter was amended by the ordinance of August 21, 1838, and by the legislative enactments of December 22, 1863, and August 7, 1888. The present constitution of the bank dates from December 27, 1888.

The charter was granted in 1814 for a term of twenty-five years, and it was renewed for the same period in 1838 and again in 1863. The law of August 7, 1888, decreed an extension provisionally for a term of fifteen years, to expire on March 31, 1904. It was provided that if notice of intention to withdraw from the arrangement was not served by the Government or by the bank two years previous to that date, the term of the charter was to run another ten years. As the Government availed itself of the notificatory privilege, a new arrangement went into effect in pursuance of the law of December 31, 1903. The term of the charter was extended for a period of fifteen years (until March 31, 1919), and it was provided that in the absence of notice of withdrawal on either part, which notice in order to be effective must be served at least two years before the expiration of the charter, there should be an extension again and again for a year. The

continuance of the Bank of the Netherlands as a joint-stock company until March 31, 1894, is provided for in the new statutes sanctioned on March 5, 1904.

The Bank of the Netherlands has its seat at Amsterdam. The ordinance of 1814 authorized it to do business in other places through correspondents or commissaries, and the ordinance of 1838 prescribed the establishment of a subsidiary bank at Rotterdam. In spite of this nothing was done toward the creation of branches during the first five decades of the bank's activity. The enactment of stringent provisions in the law of 1863 at length compelled the bank to take action in this direction. On March 31, 1907, there were (not reckoning the subsidiary bank at Rotterdam) 102 branch offices of one kind or another, variously constituted with regard to the scope of their activities.

The Bank of the Netherlands had originally an actual monopoly of note issues in the European territories of the Netherlands. The ordinances of 1814 and 1838 provided expressly that no other institution should be authorized to issue notes in the next twenty-five years. By the law of 1863 this monopoly was formally abolished, it being provided that other banks of issue might be created by special legislation and that the circulation of foreign bank notes might be legalized. No use has, however, been made of this authorization, so that the system of bank-note circulation in the Netherlands is completely centralized.<sup>a</sup>

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<sup>a</sup> In the Dutch East Indies a central bank of issue exists in the Bank of Java, at Batavia, and in Dutch Guiana there is the Bank of Surinam. The former was established in 1827 and the latter in 1864.

## *The Bank of the Netherlands*

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The Bank of the Netherlands enjoyed at the beginning various privileges besides that of note issue. In addition, the Government assigned premises to it for occupancy free of charge and subscribed to 1,000,000 florins of the original capital, which was a valuable assistance, as there was more or less difficulty at first in placing the capital stock. The privileges were materially curtailed in 1838 and they were altogether suppressed in 1863, except in so far as the exemption of the notes from the stamp tax was concerned. In 1864 the Government ceased to provide free quarters for the bank. In 1847 the Government disposed of its share in the bank's capital.

In the beginning the bank was not obliged to render any compensatory services to the State, and for a time the only profit that the Government derived from the institution was that yielded by the stock which it held and the gain resulting from the assumption by the bank, free of charge, of the functions of a fiscal agent. The law of 1863 provided for further counter obligations. The duty might be imposed upon the bank by royal decree of discharging gratuitously the functions of a receiving and disbursing agent for the royal treasury at Rotterdam and other places where there were branch offices, and the institution was to be responsible to the minister of finance. Legislation might even be enacted transferring to the bank, under certain conditions, the entire service of the royal treasury, an obligation which the bank has redeemed since 1871 by the annual payment to the Government of 100,000 florins. The bank was furthermore, obliged by the law of 1863 to lend its aid gratuitously in the preparation, issue, and withdrawal

of coin certificates (paper money), as long as the volume of such currency did not exceed 15,000,000 florins. Finally the Government reserved to itself the right of subscribing to the 1,000 new shares (1,000,000 florins) provided for in the law and to sell them to the public, the profit on the transaction to accrue to the royal treasury. The law of 1880 made it incumbent upon the bank to act as receiving and disbursing agent for the system of postal savings banks without compensation.

Additional counter obligations were prescribed by the law of 1888. The bank was to act gratuitously as receiving and disbursing agent for the Government at Amsterdam, Rotterdam, and other places where there were branch offices, and to manage the central treasury at Amsterdam without compensation. It was provided that in case the Netherlands became a party to a bimetallic league the bank should be obliged by law to buy the coin metal brought to it for sale at the coinage price, provided that such an obligation was imposed upon the central banks of issue in the other states of the union. The law obliged the bank to make advances to the Government on current account up to the sum of 5,000,000 florins, the Government to pay the regular interest on loans and to offer treasury notes as security. This provision was to be effective only in so far as the finance minister considered such advances necessary in order temporarily to strengthen the royal treasury, and so long as the available metallic reserve of the bank did not sink below 10,000,000 florins. The law of 1888 further "authorized" the bank to make advances to the Government on current account in connection with the exchange of coin certificates for standard

## *The Bank of the Netherlands*

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coin, it being provided that the fund entered in the national register of debts as a guaranty of such exchange should be assigned to the bank as collateral. This obligation was to cease if the Government proceeded to issue more than 15,000,000 florins of such currency. The law of 1888 provided that in the event of the nonrenewal of the bank's charter in 1904 one-half of the amount of the increase in the surplus between 1889 and 1904 should go to the State. By this legislation the Government was assigned a share in the current profits of the bank. Out of the net earnings an amount equal to 5 per cent of the original capital was first of all to be allotted as a dividend to the shareholders.<sup>a</sup> Of the remainder, 10 per cent was to be assigned to the surplus until this was brought up to 25 per cent of the capital. One-half of what was left was to go to the State and one-half to the shareholders until the dividends to the shareholders amounted to 7 per cent of the capital. Whatever net earnings there were after this were to be distributed in the proportion of two-thirds for the State and one-third for the shareholders. The participation of the Government in the profits was to cease as soon as it authorized any other bank to issue notes or in the event of its proceeding to issue more than 15,000,000 florins of coin certificates.

The scope of the legislation of 1888 was extended by the law of 1903. The bank was to be obliged henceforth to discharge gratuitously the functions of fiscal agent, not merely for the royal postal savings institution, but also in

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<sup>a</sup> In case the net earnings were not sufficient to provide a 5 per cent dividend the deficiency was to be supplied out of the surplus, which, however, was not to be permitted to sink below 15 per cent of the capital.

behalf of the other arrangements created by the legislature or by the Queen, and the safe-keeping of the funds of the postal savings banks and other institutions, as well as of the valuables accepted by these institutions as security, was to be committed to the bank whenever the minister of finance deemed it necessary. The bank was further to be bound (not merely "authorized"), at the request of the finance minister, to make advances to the Government on current account without interest up to the sum of 15,000,000 florins for the purpose of temporarily strengthening the royal treasury, a sufficient security in the way of treasury notes being given. This obligation was to cease when the metallic reserve was reduced to 10,000,000 florins or in the event of the issue by the Government of coin certificates after October 1, 1904. In case the Government proceeded to issue such currency after that date, or in case it conferred the privilege of note issue on some other bank, the participation of the State in the profits of the Bank of the Netherlands was to cease. The share of the Government in the profits was increased. An amount equal to 3½ per cent of the capital was first of all to go to the shareholders. Ten per cent of the remainder was to be assigned to the surplus until it was raised to the prescribed amount. Three per cent of what was left was to be allotted to the directors and commissaries, and beyond that the profits were to be distributed in the proportion of two-thirds for the State and one-third for the shareholders. In the year 1906-7 the Government's share of the profits was 3,397,349 florins. In case the privilege of note issue should not be extended, one-half of the amount by which the surplus will have been in-

## *The Bank of the Netherlands*

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creased in the period 1889-1919 is to go to the State. It is provided that the coin certificates are to be withdrawn from circulation, the bank lending its cooperation (only 10-florin bank notes to be issued in exchange). The law of July 18, 1904, made all the notes of the bank a legal tender except in the case of payments made by the bank itself.

The supervision over the bank has been exercised since 1863 by a royal commissary, whose salary, down to 1904, was paid by the bank. The management of the institution is carried on by a directorate, consisting of the president, five directors, and a secretary. The president and secretary, who are permanent officers, are appointed (and removed) by the sovereign. Since the law of 1888 the five directors have been elected (not at the same time) by the shareholders for a term of five years. The whole body of shareholders has been represented since 1863 by the general assembly. The possession of five shares entitles a person to one vote, and every additional 10 shares to one additional vote. The general assembly chooses fifteen bank commissaries, who constitute a sort of supervisory council, for a term of five years. One-fifth of the number retire each year.<sup>a</sup>

The members of the directorate and the commissaries receive a share of the profits.

The capital of the bank was originally 5,000,000 florins. It was increased by an ordinance of 1819 to 10,000,000 florins, by an ordinance of 1840 to 15,000,000 florins, by a law of 1863 to 16,000,000 florins, and by a law of 1888 to

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<sup>a</sup> Previous to 1863 six commissaries were chosen by a committee consisting of the fifty largest shareholders.

## *National Monetary Commission*

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20,000,000 florins. Any further enlargement can be effected through the channel of legislation only, whereas formerly the King could decree an increase. The legislation of 1888 provided that one-fifth of the capital might be invested in Dutch Government bonds or in other securities listed at the Amsterdam exchange or other principal European exchanges. The list of such securities is determined by the directorate and the bank commissaries. This provision regarding investment applies also to the surplus. It was not until 1888 that a surplus was declared by law to be obligatory. The legislation of that year provided that it be brought up to 25 per cent of the capital, a condition which has already existed many years.

The denominations of the bank notes were fixed by the ordinances of 1814 and 1838 at 25, 40, 60, 80, 100, 200, 300, 500, and 1,000 florins. Since 1863 only the minimum denomination (at first 25 florins, but since 1903 10 florins) is prescribed. The quantities of the various denominations of bank notes in circulation on March 31, 1907, was as follows:

Denomination.	Number of notes.	Denomination.	Number of notes.
10-florin-----	2,340,105	100-florin-----	575,447
25 florin-----	1,600,175	200-florin-----	93,961
40-florin-----	670,834	300-florin-----	65,084
60-florin-----	585,565	500-florin-----	11
80-florin-----	15	1,000-florin-----	38,311

The ordinances of 1814 and 1838 provided that the Government should fix the maximum note circulation with reference to the actual capital and resources of the bank. It was not until 1847 that it had recourse to

## *The Bank of the Netherlands*

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such action; it then fixed the amount at 52,000,000 florins. By the ordinance of February 15, 1849, the limit was set at 72,500,000 florins, and the ordinance of October 18 of the same year raised it to 122,000,000 florins, prescribing a metallic reserve of 40 per cent against the first 52,000,000 florins and one of 100 per cent against the remainder. On October 27, 1855, the limit was fixed at 150,000,000 florins, a cash reserve being prescribed of 40 per cent against the first 50,000,000 florins, one of 60 per cent against the next 50,000,000 florins, and one of 100 per cent against the remainder. On October 23, 1857, the reserve against the first 100,000,000 florins was fixed at 40 per cent. The law of 1863 suppressed the maximum limit and provided that the percentage of reserve should be fixed by royal decree. The ordinance of 1864 prescribed a metallic reserve of 40 per cent against bank notes and all other demand liabilities. The rest of the circulation is covered by bills and collaterals on loans. The notes of the bank play a great rôle in the monetary circulation of the Netherlands. In the year 1906-7 the average volume outstanding was 265,580,000 florins. The notes are redeemable on demand at the main bank, the subsidiary bank at Rotterdam, and the branch offices. The branch offices are, however, allowed to take as much time as is required to get the coin needed from the main establishment. The notes are accepted in the payment of dues to the Government and are not subject to the stamp tax. The bank is not responsible in the case of the loss or destruction of the notes. Where there is reason to suspect the existence of some fraud the bank may demand a receipt from a person

offering notes for redemption. Since 1863 the bank has been authorized to issue drafts drawn by one of its offices upon another. It must keep a metallic reserve of 40 per cent against the aggregate volume of such drafts outstanding. The use of such drafts was for a long time confined within narrow bounds by a stamp tax of 5 cents (Dutch, equal to  $\frac{1}{20}$  of a florin) per florin. Since 1883, however, the stamp tax has been only 5 cents on each draft irrespective of the amount. A draft is not permitted to circulate more than eight days. In the year 1906-7, 55,075 drafts were issued to the aggregate amount of 381,590,000 florins.

The charter of 1814 provided for the following kinds of business: The discounting of bills; the making of loans on stocks and goods; the purchase and sale of coin and the precious metals; the taking of deposits on current account. These branches of business have been retained in a greatly amplified form. In 1838 the bank was authorized to discount commercial paper other than bills. In 1863 the discount business was extended so as to embrace debentures redeemable in the kingdom and maturing within three months and the coupons of foreign government bonds, as well as the securities of private corporations or companies. Promissory notes and domestic bills are not discountable if their date of maturity is more than three and one-half months from the date of discount. Bills drawn in Europe on America are not allowed to have more than three months to run before maturity. Bills drawn on China, Sumatra, British India, and Australia must be payable within six months from the date of acceptance. For promissory notes and for

## *The Bank of the Netherlands*

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domestic bills having more than three months to run the rate of discount is, as a rule, higher by one-half of 1 per cent than in the case of other bills. Bills drawn by the agents of mercantile concerns and credit institutions in the Dutch East Indies (with the exception of the Dutch Trading Company) on the offices of such concerns in the Netherlands are discountable only if they are payable within ten days after sight or two months after date of acceptance. All paper that is to be discounted must bear the signature of an individual or firm in the Netherlands or the Dutch colonies and must be payable at one of the branches of the bank. Paper payable at a place where the bank does business only through a correspondent is subject to a super-discount of one-eighth of 1 per cent.

Foreign securities may be offered as collateral for loans. The charter of 1814 fixed 5 per cent as the maximum rate of interest in loan transactions. In 1838 the limit was abolished, the usury law of 1807, however, not permitting the rate to be above 6 per cent. The limit thus imposed was abolished by the legislation of 1857. Advances are, as a rule, made for a term of three months, but where stocks are offered as collateral a renewal of the loan for another three months may be granted. There are also "short loans," for eight days, on securities and goods.

In its dealings in the precious metals no fixed purchase price is prescribed for the bank. The price paid for a kilogram of pure gold since 1881 is 1,648 florins, the amount obtained at the mint after deduction of the seigniorage being 1,647.87 florins. The higher price paid

by the bank has had the effect of bringing to it the bulk of the gold that is imported, so that the coinage of gold in the Netherlands is done mainly for account of the bank.

The current-account business of the bank was restricted by the charter of 1814 to the funds of the Government and the public authorities. In 1838 this restriction was removed, but the public has, nevertheless, availed itself only to a small extent of the facilities offered by this department of the bank's business, as they have not been sufficiently ample.

To the four branches of business above described the bank added a fifth branch in 1869, the safe-keeping of valuables. At first only "closed deposits" were accepted; that is to say, sealed packages not exceeding 50 kilograms in weight, with extreme dimensions, in centimeters, of  $70 \times 70 \times 50$ . Since 1880 "open deposits" have been accepted; that is to say, securities in loose parcels. Since 1889 the bank has attended to the cashing of the coupons, charging a commission of one-fourth of 1 per cent. The fees for safe deposit of valuables are moderate. Closed packages are taken only at the main office and in the offices at Rotterdam, The Hague, and Groningen. Open packages are taken at the agencies and subagencies.

The law of 1888 added a sixth branch of business, the purchase and sale of bills payable in foreign countries and of other foreign paper bearing two or more good signatures. The aggregate amount of money invested in such foreign paper is not to exceed the metallic reserve for more than fourteen days in succession. The bank is not permitted to engage in other kinds of business than those enumerated. Previous to 1848 the operations of the bank

# The Bank of the Netherlands

were on a very small scale. After that, under the influence of the new secretary (later president), Dr. W. C. Mees, and as a result of the reform of the coinage (1847-1852), the diminution of the paper currency, and the introduction of a limited amount of publicity, business became somewhat more active. Nevertheless the bank remained, down to 1863, a local Amsterdam institution. With the establishment of branches, which was made obligatory by the law of 1863, a new period in the development of the bank's activities was inaugurated, in the course of which the Bank of the Netherlands attained to a very important position in the monetary and credit systems of the country.

## *Development of the business of the Bank of the Netherlands since 1864.*

[In millions of florins.]

Year.	Notes in circulation.	De- posits (cur- rent ac- count).	Me- tallic re- serve.	Aggre- gate of dis- counts during the year.	Aggre- gate of loans on col- lateral during the year.	Gross profits.	Average rate of discount for bills.	Average rate of discount for promis- sory notes.	Divi- dends.
1864-65----	105	34	82	239	-----	4.3	5.2	5.61	19.7
1875-76----	184	49	151	396	145.7	4.4	3.2	3.7	21.4
1880-81----	194	19	150	287	178.6	3.1	3	3.5	14.3
1890-91----	208	13	119	417	227.1	4.4	3.2	3.52	9.3
1900-1901--	223	8.1	128	387	238.2	4.4	3.5	4	10.4
1901-2----	228	7	140	329	225	3.5	3.1	3.6	9.4
1902-3----	231	5.8	136	354	245	3.8	3.02	3.52	9.7
1903-4----	235	6.4	130	410	224.4	4.5	3.5	4	10.9
1904-5----	247	7.7	144	405	200.1	3.5	3.08	3.58	7.8
1905-6----	269	6.4	152	428	247.3	3.6	2.7	3.2	8
1906-7----	270	5.6	135	449	289.1	6.2	4.66	5.16	11.6



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# The Austro-Hungarian Bank

BY

PROFESSOR ZUCKERKANDL

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[From Conrad's *Handwörterbuch der Staatswissenschaften*, 3d edition]

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## I.—THE CHARTERED AUSTRIAN NATIONAL BANK (1816).

The Austro-Hungarian Bank was instituted in 1878 as the successor of the Chartered Austrian National Bank. This had been established in 1816, mainly for the purpose of undertaking the withdrawal from circulation of the paper currency of the Austrian Government. This paper currency consisted of the so-called “redemption notes” (*Einlösungsscheine*), which had been issued in virtue of the imperial patent of February 20, 1811, in order to take the place of the then outstanding government paper money,<sup>a</sup> and the aggregate volume of which was 208,715,925

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<sup>a</sup> Redeemed at the ratio of 5 florins of the old paper for 1 florin of the new.—TRANSLATOR.

florins, and of the so-called "loan (advance) notes" (*Antizipationsscheine*), which were first issued in virtue of the imperial patent of April 16, 1813, to the amount of 45,000,000 florins and the volume of which had risen by a succession of increases, which were not announced to the public, to 470,000,000 florins. The redemption notes were styled in the law "Viennese currency" (*Wiener Währung*). The *Antizipationsscheine* were placed legally on the same level with the redemption notes. Both kinds of money were forced currency, there being no obligation on the part of the Government to redeem one or the other. They were at the same discount with respect to coin, the premium on which in the month of May, 1816, was on an average such that 100 florins "convention coin" (*Konventionsmünze*), the standard Austrian coin (a Cologne mark of pure silver being coined into 20 florins), was worth 346<sup>a</sup> florins paper currency.

Two imperial patents of the date of June 1, 1816 (not quite a year after the termination of the Napoleonic wars), decreed the voluntary and complete withdrawal of the government paper currency and the establishment of a bank of issue, styled from the outset the "Chartered Austrian National Bank," at which institution alone the paper might be redeemed. Two methods of redemption were provided for. In the first place paper currency to the amount of 140 florins, or of a multiple of 140 florins, might be presented at the bank and the holder would receive in exchange five-sevenths of the face value in government bonds, bearing interest payable in standard ("convention") coin at the rate of 1 per cent (one 100 florins

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<sup>a</sup> By a misprint the figure in the original is 446.—TRANSLATOR.

## *The Austro-Hungarian Bank*

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bond for the 100 florins taken out of each 140 florins); and two-sevenths in bank notes, which the National Bank was obliged to redeem, at any time on presentation, in specie. The second way was by means of the purchase of a share of the National Bank by the payment of 2,000 florins in paper and 200 florins in convention coin so long as the 50,000 shares of the National Bank were not all disposed of. The paper thus handed in at the bank in the one way or the other was to be destroyed, and in place of the paper money paid in as capital by the purchasers of the shares the bank was to receive an equal amount (nominal value) in 2½ per cent government bonds. The bank was to come into existence as soon as 1,000 shares were paid in, but previous to this, as early as July 1, 1816, business was to be started under a provisional management instituted by the Government, and the operation of withdrawing government currency from circulation in exchange for government bonds and bank notes was to begin. The bank was to proceed at once to redeem its notes in coin, to manufacture bank notes, to issue shares on the payment of the above-mentioned sums, and to destroy the government currency handed in. The redemption of the bank notes in coin was to commence immediately with their issue, and no larger volume of notes was to be issued than was warranted by the supply of coin on hand. To provide for the redemption of the bank notes issued in exchange for government currency, it was decreed in the first of the two imperial patents of June 1, 1816, that all "moneys due from foreign powers pursuant to treaty obligations and all available coin in the imperial treasuries" be turned over to the

bank, and the second patent declared that the coin handed over by the State to the bank for the purpose of redeeming the government currency was not to be repaid.

The activity of the National Bank, in addition to the redemption of the government currency and the administration of the sinking fund for the government securities issued in connection with the redemption of the paper currency, was to embrace the discount business and eventually the granting of credit on mortgage. The payment into the treasury of the bank of 200 florins standard coin in the purchase of each share was to provide the necessary working capital. The returns to the stockholders were not to be restricted, however, to the profits of the discount business. The government bonds, which, as we have seen, were assigned to them in exchange for the government currency paid into the bank in the purchase of their shares, was to yield them an annual interest, payable in standard coin, at the rate of  $2\frac{1}{2}$  per cent of the nominal value of the paper money paid in. These obligations were to be called in by the Government in yearly installments.

The National Bank was invested by the imperial patents of June 1, 1816, with extensive privileges. It had the exclusive right of issuing bank notes, which had the advantage of being made receivable at all the public treasuries and of being the sole medium in which certain specified taxes were to be paid, and which were "secured by a special mortgage on all the mines belonging to the State." It was provided that the notes received at the public treasuries were not to be presented at the bank for redemption. The bank had, furthermore, the exclusive right to establish (with the imperial sanction) branches or discount

## *The Austro-Hungarian Bank*

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offices wherever it seemed advantageous, while no other concern was permitted to establish a "discount institution." The absolute obligation was, on the other hand, imposed upon the bank to redeem its notes at all times, and the notes might be issued only for the purposes mentioned in the imperial patents and never without due regard for the amount of coin available and the absolute assurance of their value. The shareholders were made responsible for the redemption ("the thorough and uninterrupted security") of the notes to the full amount of the money paid in by them. There were no precise provisions regarding a metallic cover for the notes.

The ministry of finance furnished the coin and the bank notes and the Government undertook to defray the running expenses. It was, of course, of the greatest importance with respect to the success of the whole operation that the provisional management should be provided at the opening of the institution and in the initial period of its activity with a large supply of standard coin. The Government had accorded unusual advantages to the holders of the paper currency. For every 2,000 florins paper money paid in for a share the bank got 2,000 florins in  $2\frac{1}{2}$  per cent government bonds, the interest on which was payable in standard coin, which was a much greater value than the shareholders were entitled to with reference to the premium on silver, 100 florins in standard coin having been worth on an average 346 florins in paper in May, 1816, and 283 florins in the month of June. In like manner the exchanging of government notes for 1 per cent bonds (to the extent of five-sevenths of the nominal value of the notes) and bank notes (two-sevenths of the

amount of the government paper) was a no less profitable transaction. A person presenting 140 florins in government notes at the bank got in exchange a 1 per cent government bond, the interest on which was payable in coin, and 40 florins in bank notes, which the bank was obliged to redeem at any moment in coin. Assuming that the bond was worth 20 florins in standard coin, 60 florins in coin would be received in exchange for 140 florins in government currency, or, assuming that the bond would bring 15 florins in coin, the sum (in coin) received in exchange would be 55 florins. The quotations to which these figures would correspond would be 233 and 254 florins paper for 100 florins coin, respectively. Even at the figure to which the premium on coin declined at the close of June, 1816 (261 florins paper for 100 florins coin), it would still pay to present the government notes for exchange. But even if there had been no anticipation of profit, it would have been likely that the public would proceed to exchange large amounts of the hitherto irredeemable government notes at the bank for bank notes and government bonds bearing interest payable in coin. It was likewise almost certain that a great many persons would immediately present the bank notes received in exchange for government notes for redemption in standard coin.

The financial administration did not take adequate account of these contingencies when the National Bank was opened on July 1, 1816. The supply of coin placed at its disposal being insufficient, the bank management proceeded to restrict the redemption of the government currency, no more than 7,000 florins being accepted from any one party from July 8, and applications for redemp-

## *The Austro-Hungarian Bank*

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tion being required to be made in writing from August 5. The direct redemption at the bank was suspended on August 18, and from August 26 the buying up of government notes was done at the Bourse in the name of the bank. These purchases were discontinued after January 25, 1817. Already in October, 1816, the Government had proceeded to take a step which meant a departure from the plan of redemption embodied in the imperial patents of June 1, 1816, through the issue of a loan, by means of which 130,000,000 florins of paper currency was called in. The total amount of government paper currency withdrawn from circulation by the issue of bank notes and 1 per cent government bonds was 46,325,000 florins.

In the meanwhile the organization of the National Bank was being effected altogether along the lines laid down in the imperial patents of June 1, 1816. Its statutes received the approval of the Government on July 15, 1817, and on January 19, 1818, the provisional management was superseded by an elected board of directors. In the enumeration of the various kinds of business to be carried on by the bank there is no longer any mention of the withdrawal of the government paper currency from circulation. To the discounting of commercial paper (bills drawn on or payable in Vienna) and loans on mortgages<sup>a</sup> the new statutes added the following kinds of business: The issue and redemption of "drafts" drawn by the bank on itself (bank notes); the giro business (the effecting of payments by transfers from one account to another), in which, however, the bank did not engage

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<sup>a</sup>The bank was not to embark in the mortgage business until later on.

during the period of its first charter; the taking of deposits; and the making of advances and loans on movable property. The notes issued were to be redeemable in standard ("convention") coin on demand. The bank statutes did not prescribe any ratio between circulation and metallic reserve, nor was there any mention of an obligation on the part of the bank to provide a cover for its notes in the way of readily convertible securities. The bank was permitted to loan money on bullion, articles made of the precious metals, government securities bearing interest payable in standard coin, etc. Such loans were to be limited to three months. One kind of business which the bank carried on that was not enumerated in the statutes was the issuing of ordinary drafts.

The amount of the capital stock was left as it had been originally fixed, but the shares were reduced to 1,000 florins paper and 100 florins coin, so that the number of shares was doubled. The provision was retained by which the bank was to receive in exchange for the sums paid in by the purchasers of the shares in government paper currency an equivalent nominal amount in 2½ per cent government bonds, the interest on which was payable in silver. These securities were not negotiable and were to be redeemed by an annual payment to the bank of 500,000 florins in standard coin, which was to cancel 1,000,000 florins of the Government's obligations.<sup>a</sup> The bank was not allowed freedom of action in the disposition of its net profits. Thirty florins per share was to be paid out annually as an ordinary dividend. One-half of the net profits beyond

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<sup>a</sup>The Government was to continue to pay the bank the amount of the interest on the paid-off bonds, the sums thus paid being applied to the further reduction of the Government's debt.

## *The Austro-Hungarian Bank*

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that was to be applied to the creation of a surplus fund. After the lapse of one or two years, however, this restriction was rescinded, and from 1820 on, the committee of the shareholders determined the dividends after a preliminary conference on the part of the managers with the ministry of finance. The management of the bank consisted of the governor and his deputy (both appointed by the Government) and of twelve directors, chosen by the committee of the shareholders, made up of the one hundred shareholders having the largest number of shares. The committee was empowered to examine the statements, to inquire into the management of the bank, to resolve upon changes in the statutes suggested by the board of directors, to call upon the directors for information regarding the disposition made of the funds, etc. The supervision of the Government was exercised through a commissary, who was allowed to state his views at the meetings of the committee of the shareholders and the board of directors. If he protested against a measure on the ground of its being opposed to the statutes of the bank or to the public welfare, its operation was suspended. The bank was granted the privilege of issuing notes throughout the whole extent of the monarchy. This was not an exclusive privilege, but, as a matter of fact, the bank enjoyed a practical monopoly of note issue. The notes, which were not a legal tender, were to be accepted at all the government offices in place of standard coin on a par with such coin. The charter of the bank was to expire in twenty-five years or else when the  $2\frac{1}{2}$  per cent government bonds were all redeemed. A new charter went into operation on October 28, 1841.

## II.—BUSINESS OF THE OLD NATIONAL BANK WITH THE GOVERNMENT.

In January, 1817, the National Bank engaged in the business of discounting commercial paper. Out of the proceeds of this and the interest on the  $2\frac{1}{2}$  per cent government bonds (which had been assigned to the institution in exchange for the sums paid in as capital in paper currency) dividends were paid to the shareholders for the years 1816 and 1817. The managers now proceeded to the remaining kinds of business provided for in the statutes of the bank (with the exception of the giro transfer and loans on mortgages) and also to the issue of drafts. But what was of greatest importance with respect to the institution and the interests concerned with a bank of issue were the operations undertaken for the Government. These were the redemption of the paper currency and the discounting of treasury bills. In connection with the former, the issue of shares was suspended at the close of 1819, when the total number disposed of was 50,621, about one-half of the number constituting the nominal capital therefore remaining unsold.

In 1819 the Government took up once more the original plan of redeeming its paper currency through the agency of the bank. The conditions of the redemption and the mutual obligations of the State and of the bank were fixed otherwise than in the imperial patents of 1816. The bank, by an agreement dated March 3, 1820, undertook to redeem the paper currency for the Government, the redemption to be effected without compulsion at the ratio, unalterably fixed by the Government, of 100

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florins convention coin for 250 florins paper. The aggregate of the paper currency in circulation at that date was estimated by the ministry of finance at 449,716,000 florins (the number being rounded off to 450,000,000 florins). The Government, on its part, assumed the following obligations: To buy back at once the 2½ per cent bonds, amounting (a fraction having been redeemed) to 23,232,000 florins convention coin; to take over the 49,379 shares which had not yet been issued at the price of 610 florins convention coin, the amount to be paid being thus 30,121,190 florins; to hand over to the bank in cash the sum of 40,000,000 florins convention coin, 10,000,000 florins at once and 30,000,000 florins in installments, as the progress of redemption should demand; to assign to the bank for the remaining 140,000,000 florins (180,000,000 florins being the total sum required for the redemption of the 450,000,000 florins of paper currency at the ratio fixed—100 to 250) 4 per cent nonnegotiable government bonds, along with which the bank was to receive as a subsidiary mortgage 5 per cent government bonds (100 florins for each 70 florins coin due the bank), negotiable in the event of the inability of the Government to make the promised payments; to redeem the 4 per cent bonds by means of a 1 per cent amortization. By the close of 1823 the Government had delivered to the bank the 40,000,000 florins coin and paid the 23,232,000 florins for the 2½ per cent bonds (the paid-in capital represented by the 50,621 shares being made equivalent thereby to 600 florins coin per share).

In 1821 the state of the imperial finances became worse in consequence of an unexpected expenditure for military

purposes in Italy and the Government sought to diminish the burdens assumed in the agreement into which it had entered on March 3, 1820. The managers of the bank agreed to the cancellation of the engagement on the part of the State to take over the 49,379 shares. On November 30, 1822, a new agreement was entered into. At this date the bank had redeemed in all about 184,000,000 florins Viennese currency, for which it had issued bank notes to the amount of 74,000,000 florins and had received from the Government 40,000,000 florins in convention coin and 60,000,000 florins (convention coin) in 4 per cent bonds, so that it had in its possession the cover for 250,000,000 florins Viennese currency. For the remaining 200,000,000 florins the Government would have had to turn over to it in installments 4 per cent bonds to the amount of 80,000,000 florins. In order to avoid the expenditure in the way of interest on this sum, the ministry of finance substituted for its previous engagement an obligation to turn over to the bank 30,000,000 florins in coin, to serve as security for its notes issued in the redemption of the government currency, it being at the same time stipulated that the amortization in the redemption of the 4 per cent bonds be suspended until 1837 and that the sums which the bank would be required to pay out in the redemption of the remaining 125,000,000 florins government currency (the maximum amount needed would be 50,000,000 florins convention coin, in case all the paper was presented for redemption) be regarded by the bank as an advance made to the Government in the shape of a noninterest-bearing loan.<sup>a</sup> The 30,000,000 florins were paid to the bank in the years 1824-

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<sup>a</sup> The bank was assigned 5 per cent bonds as a subsidiary mortgage.

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1826. The redemption of the paper currency went on from year to year in decreasing proportions. The notes were destroyed with the exception of what was needed in connection with such government securities the interest on which was payable in "Viennese currency."

Next to the redemption of the government paper currency, the most important business carried on by the National Bank was the discounting of drafts of the imperial treasury. As government expenditures had often to be made then, just as now, before the revenues destined to cover them had come in, and as, moreover, the superfluous funds accumulated in the provincial treasuries could in those days not be placed quickly enough at the disposal of the central imperial treasury, the ministry cast about for a means of overcoming these not very formidable obstacles, and it naturally bethought itself of the idea of invoking the aid of the bank. The plan adopted in the agreement of February 28, 1822, was that the bank should discount drafts drawn by the central imperial treasury on the revenue offices in Vienna and such of the provincial towns in which was located one of the exchange offices (*Bank-Verwechslungskassen*) which existed in connection with the government treasuries and whose function it was to exchange bank notes, transact business in connection with drafts, and redeem government notes. The rate of discount was to be the prevailing rate, and the term of the drafts to be discounted was not to exceed three months. Out of this relation a permanent indebtedness to the bank was soon developed, inasmuch as the revenues of the Government did not cover the expenditures. Under the three-months' discount,

renewed again and again, an actual loan on the part of the bank to the Government was concealed. The amount of the credit thus granted increased from 6,000,000 florins in 1822 to 30,000,000 florins in 1835. In 1842 it was 24,000,000 florins, and in 1843-1845, 20,000,000 florins, and it rose again in 1846 to 30,000,000 florins, and in 1847 to 50,000,000 florins. The interest was 5 per cent in 1822, was reduced to 4 per cent in 1823, and after 1834 was 3 per cent. These drafts of the imperial treasury were, of course, kept out of the channels of ordinary financial intercourse.

The two kinds of business which we have here described were highly profitable for the bank. The interest on the 4 per cent bonds yielded, from 1823 to 1836, an annual revenue of 2,281,190 florins, from which, after the amortization had been resumed in 1837, there was a decline to 1,646,941 florins in 1847. The annual profits from the discounting of the treasury drafts rose from 19,583 florins in 1822 to 612,141 florins in 1826 and to 1,046,909 florins in 1839, and between 1826 and 1847, with the exception of two years, was never less than 600,000 florins. This splendid showing of the bank down to 1848 must be ascribed entirely to the payments made by the Government. The business done with the Government was for the shareholders just what they were craving for, but nevertheless this whole business relation can not be designated as anything else than altogether mistaken and mischievous. On the strength of it the bank issued large volumes of notes without metallic cover. By reason of its relatively small cash reserve, it would not have been able in a political or economic crisis to redeem its notes in the event of a run upon it.

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The Government's indebtedness was not calculated for a brief term, a gradual liquidation, at best, being all that was contemplated, while a severance of the connection through large repayments could not have been thought of. In the period from 1823 to 1841, as the annual statements show, there was at no time a one-third metallic reserve. As a general thing there was not even a one-fourth reserve, and we find such ratios as 1 to 6.37, 1 to 7.10, and 1 to 10.77. Considering that in the case of the great bulk of the notes there was no regular reflux such as is characteristic of sound banking, even a one-third reserve would barely have been sufficient. The extraordinary nature of the whole situation is revealed by the fact that the statements regarding the condition of the bank (circulation, reserve, indebtedness of the Government) were withheld even from the committee of the bank, remaining a bureaucratic secret of the directors and a few individuals connected with the bank and the finance administration. In the addresses delivered by the governor at the annual meetings of the committee the discounting of the drafts of the imperial treasury was not discussed. The redemption of the government paper currency could, indeed, not be passed over in silence, as information regarding it had to be given to the public. The governor felt it imperative to dwell upon the fact that an arrangement had been entered into with the Government in regard to this matter, but he refrained from going into particulars. When at a meeting of the committee of the shareholders, on January 13, 1823, a member put a question regarding the new agreement with the Government, the details of

which had not been communicated to the committee, the assembly resolved, with only three dissenting votes, after the imperial commissary had called attention to the danger involved in replies to such inquiries, that further information was unnecessary.

### III.—THE SECOND CHARTER OF THE NATIONAL BANK (1841).

The various kinds of business permitted in its statutes were carried on by the bank until 1841, with the exception of the giro business (payments effected by transfer from one account current to another), in which it did not engage until 1842. In addition to this, it was engaged in the issue of drafts, a branch of business not mentioned in the statutes of 1817. The discount business and the granting of loans were, of course, of more importance than the other kinds of business (the former considered apart from the matter of the drafts of the imperial treasury). The rate of discount was at the outset (January, 1817, to January, 1818) 9 per cent; from May, 1818, to October, 1829, it was 5 per cent; then until March, 1831, it was 4 per cent; from March, 1831, to April, 1833, it was 5 per cent; after that it was 4 per cent. The changes from 1829 on were made at the behest of the minister of finance. In the loan business the rate of interest was reduced in 1819 from 6 to 5 per cent and subsequently followed the changes in the rate of discount.

The aggregate of commercial discounts increased from 9,000,000 florins at the close of 1835 to 19,300,000 florins at the close of 1836. The volume of notes outstanding issued in connection with discounts and loans amounted on June

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30, 1836, to 26,500,000 florins, and the total circulation at that date was 154,300,000 florins, while the cash reserve was only 20,200,000 florins. At the close of 1840 the discounts aggregated 31,300,000 florins while the metallic reserve had sunk to 15,500,000 florins. Those who understood the precise import of the figures of the bank statements condemned the new way of carrying on the discount business, the more that they were convinced that the managers favored a few large commercial houses, that the purpose for which the bank notes were wanted was not scrutinized, and that the rate of discount was kept down purposely in order to benefit the large customers of the bank. In the new charter, that of July 1, 1841, virtually the entire management of the bank was placed under the control of the ministry of finance.

The ministry was persuaded that the best security for the proper conduct of the institution lay in a greatly extended governmental control, especially as, under the circumstances, it was not practicable to prescribe in the statutes a ratio of metallic reserve or a cover for the notes in the form of readily convertible securities. It was evident that the bank had not been successfully managed in recent years and had more than once been brought into a dangerous situation.

The new statutes, which went into effect on October 28, 1841, provided that the bank management should from time to time determine how large a sum should be devoted to discounts and loans, but that the new adjunct government commissary should see to it that the amount was not transcended, that the commercial paper was safe, and that there was no favoritism. It was to be the duty of the

directors to fix from time to time such a ratio of circulation to metallic reserve as was calculated to insure the redemption of the notes at their face value in silver coin on demand. The fixing of this ratio, however, and every change in the ratio, was to be subject to the sanction of the ministry of finance. In like manner, changes in the rate of discount and of interest on loans were to be submitted to the imperial financial administration. The directors were no longer to be chosen by the committee of the shareholders, but were to be appointed by the Emperor out of a list of candidates furnished by the committee. The declaring of an "extraordinary" dividend (one in excess of 30 florins per share) was to require the sanction of the ministry of finance. The bank was invested with the exclusive privilege of note issue throughout the monarchy. It was authorized to carry on the business of issuing drafts, but was no longer to grant loans on real estate. The provision in the previous charter interdicting the establishment of a discount institution at any place where there was a branch of the bank was dropped. The new charter was to expire at the close of 1866, but it was provided that it might be renewed, with the necessary amendments, should the committee of the shareholders apply for such renewal.

Order was speedily restored in the course of the year 1841 by a reduction in the amount of commercial discounts, and, with the view of avoiding a recurrence of the former unsound conditions, the limit of the reserve ratio was fixed at 1 to 6. The succeeding years, under the new régime, witnessed an improvement in the condition of the bank. The debt of the Government, however, on account

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of drafts discounted, reached in 1847 the sum of 50,000,000 florins. At the close of that year the aggregate of discounts was as much as 43,600,000 florins. The bank was able at this time to maintain a metallic cover for its note circulation, amounting to 218,900,000 florins, at the ratio of 1 to 3½, which was a great remove from the limiting rate of 1 to 6.

With the close of 1847 terminated a thirty-year period of the administration of the bank under its own managers, and the shareholders and the public might contemplate with a feeling of satisfaction what had been accomplished in this stretch of time. In its bank notes the institution had placed at the disposal of the people an unimpeachable circulating medium. Through its cooperation the government paper money ("Viennese currency") had been almost entirely called in, so that the Austrian monetary system since 1820 had been on a stable basis. Along with this there were splendid returns. Since 1824 the dividends had never been less than 3,000,000 florins, and there were five years in which they exceeded 4,000,000 florins. The capital of 30,372,600 florins paid, therefore, more than 10 per cent, and the shares, which had been raised to 600 florins convention coin by the Government and not by the imbursements of the shareholders, went up as early as 1825 to 1,200 florins, in 1837 to above 1,400 florins, and in 1840 to above 1,500 florins, a level maintained ever afterwards. A closer inspection of the figures, however, by reason of the relations with the Government above described, will tend to produce a less favorable impression. The greater part of the profits of these thirty years represented interest paid by the Government on its indebtedness. Even in the relatively favorable situation at the close of 1847, out of a total

circulation of 218,900,000 florins, the volume of notes issued in connection with regular discounts and loans amounted to no more than 53,700,000 florins, while the Government's debt was 126,700,000 florins. If during these thirty years, when its condition was generally much less favorable and its discount policy often unsound, the bank was enabled to maintain specie payments, this was due to the fact that the periodical statements were kept secret and that there was no protracted political crisis.

#### IV.—THE NATIONAL BANK FROM 1848 TO 1859.

The period from 1848 to 1859 was the most stirring in the history of the National Bank. In consequence of the revolution of 1848 and the war in Italy it was forced to suspend the redemption of its notes and was repeatedly called upon to make large loans to the State. The resumption of specie payments on the part of the bank, which the Government sought to bring about, could not be permanently effected on account of the large expenditures entailed by Austria's foreign policy and the unfortunate war of 1859, in order to meet the cost of which the bank placed its resources at the disposal of the Government.

At the beginning of March, 1848, the management resolved, with the sanction of the ministry of finance, in order to restore confidence in the bank, which had been shattered by political events, to publish every month a statement of its condition. The statement for February 29, 1848, showed a cash reserve of 65,000,000 florins, a circulation of 241,100,000 florins, and an indebtedness on the part of the Government of 81,300,000 florins. The fact was concealed that the figures of discounts included 45,000,000 florins of treasury drafts. But such

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as it was, the information sufficed to show that the bank was not in a position to redeem the outstanding notes without speedy and effectual aid from the Government. By the middle of April the reserve had dwindled down to 48,600,000 florins. The Government now decreed the prohibition of the exportation of Austrian silver and gold coin,<sup>a</sup> made the bank notes a legal tender, and authorized the bank to issue notes of the denominations of 1 florin and 2 florins.<sup>b</sup> The bank was empowered to restrict the amount of coin paid out in exchange for notes to any one person at one time to 25 florins, but at the close of May, 1848, even this limited redemption had to be suspended.<sup>c</sup>

In order to meet the enormously increased extraordinary expenditures of the State in the years 1848 and 1849, as well as to supplement the diminishing ordinary revenues, the Government was obliged to come to the National Bank for loans, and the management, under the stress of the dire political conditions, was of course ready to grant what was asked, before and after the suspension of the redemption of the notes. The paper currency issued by the Government was a particular burden for the bank, as it accumulated there. The new indebtedness of the Government to the bank,

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<sup>a</sup> The prohibition was revoked in September, 1848.

<sup>b</sup> The smallest denomination had hitherto been 5 florins.

<sup>c</sup> The bank redeemed its notes after this occasionally for the benefit of the Government, of communes, corporations, and of private individuals, paying out in this way, between 1848 and 1855, nearly 100,000,000 florins in coin. There is no space to speak of the various kinds of paper currency successively issued by the Government at this time, some of which were a legal tender and others not. The premium on silver florins in 1848 reached 17 per cent. In the nine years, 1849 to 1857, the average percentages were as follows: 14, 20, 26, 19½, 10½, 28, 21, 4½, 5½.

together with the government currency lying in its vaults, amounted on September 1, 1849, to 99,591,048 florins. It was arranged that 60,000,000 florins should be paid back out of the proceeds of a 4½ per cent government loan and 24,000,000 florins out of the war indemnity of the Sardinian government. By the close of 1851 this indebtedness was reduced to 7,500,000 florins. In 1852 the debt of 50,000,000 florins, represented by the permanent advances of the bank in the way of the discounting of the drafts of the imperial treasury, was reduced to 37,000,000 florins. These two separate debts and the debt to the bank represented by the 27,000,000 florins of new government paper currency that had accumulated in its vaults were consolidated into a single debt of 71,500,000 florins bearing interest at the rate of 2 per cent. By the close of 1853 this debt was reduced to 55,000,000 florins.

In 1854 the ministry of finance entered into an agreement with the National Bank by which that institution was to redeem all of the government paper that was a legal tender in its own notes. The amount was to be repaid in annual installments of not less than 10,000,000 florins (to be taken out of the receipts of the customs, the payments to be in coin and paper in the same ratio as that represented in such receipts). This was speedily followed by a thorough-going measure designed to place the whole monetary circulation once more on a sound basis and in particular to bring about the redemption of the bank notes. For this purpose (as well as to cover the extraordinary expenditures of the Government), an imperial patent, dated June 26, 1854, decreed the institution of a voluntary loan (a "national" loan) of not less than

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350,000,000 florins and not more than 500,000,000 florins. Out of the proceeds of this loan, it was arranged that so much should be turned over to the bank up to August 24, 1858, as would, in connection with the regular payments made on account of the original debt of the Government and the yearly payment of 10,000,000 florins out of the customs receipts, reduce the total indebtedness of the Government at that date to 80,000,000 florins. Within this interval of time, at a date to be fixed by the ministry of finance, the bank was to resume the redemption of its notes. But even this strenuous measure, as was soon apparent, was destined to fail of its effect with respect to the resumption of specie payments by the National Bank. The large sums expended for military preparations in connection with the Eastern War obliged the Government to borrow from the bank in 1854 the sum of 80,000,000 florins and in 1855 an additional 20,000,000 florins. The attempt to restore to health the monetary system in Austria, the success of which was being assured by the national loan, thus came to naught. The finance minister, Freiherr von Bruck, had to start all over again with the task of setting the monetary circulation to rights. The debt of 55,000,000 florins (the sum to which the indebtedness of the Government represented in the above-mentioned consolidation of 1852 had been reduced) and the 100,000,000 florins represented by the fresh loans from the National Bank were consolidated by the agreement of October 18, 1855, to a new noninterest-bearing debt of 155,000,000 florins and imperial domains to the value of 156,000,000 florins were assigned to the bank, the revenues derived from which and the proceeds from whose sale should go toward the diminution of

the debt. The sum due the bank on account of the withdrawal from circulation of the new government paper currency (in exchange for which the bank had issued its own notes), amounting to 44,200,000 florins, was repaid out of the proceeds of the national loan, this indebtedness being extinguished in 1857. The reduction of the debt of 155,000,000 florins proved to be an extremely slow operation, so that the arrangement of October 18, 1855, turned out to be a very unfavorable one for the bank, while it was altogether inadequate with respect to the main object in view.

In the meanwhile, however, the reduction of the period of time within which it might be possible for redemption to become an accomplished fact was being effected in another way.

As early as 1853 the National Bank had increased its capitalization by the issue of the 49,379 shares lacking in order to make up the original 100,000 shares at the price of 800 florins in bank notes. It proceeded in 1855 to augment still further the capital thus greatly enlarged by the issue of an additional 50,000 shares, which were to be paid for at the rate of 700 florins in silver coin or an amount of bank notes corresponding to the premium on silver. This increase would amount, therefore, to 35,000,000 florins in silver coin. The issue of the new stock, which took place in connection with the creation by the bank, at the order of the Government, of a mortgage department, brought about a very considerable increase in the stock of coin, which at the close of 1856 amounted to 87,200,000 florins, there being in addition foreign bills to the amount of 10,900,000 florins. The minister of finance now felt that a

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not distant date should be fixed for the resumption of the redemption of the bank notes. The monetary convention of January 24, 1857, between Austria and the states of the German Zollverein which had entered into the monetary convention of 1838 provided that the parties to the agreement were to bind themselves not to issue paper money invested with the character of a legal tender (or allow such money to be issued) unless arrangements were made enabling the holder to exchange it at any time on demand for full-weight silver coin.<sup>a</sup> The imperial decree of August 30, 1858, ordered the National Bank from the first day of November of that year to issue only bank notes bearing a promise to pay in Austrian standard coin, in denominations of 1,000, 100, and 10 florins. The notes payable in Austrian standard coin were to be redeemable on demand at the main office of the bank in Vienna in full-weight silver coin. The volume of such notes outstanding was to be covered by a one-third reserve of legal silver coin or silver bullion or in part (under certain conditions, with the sanction of the finance minister) of gold coin or gold bullion and (for the remainder of the sum total) by securities legally discounted or furnished as collateral. Austrian-standard notes were to be a legal tender in all cases where payment was stipulated for in money of that standard. As fast as these notes were issued the "convention-coin" notes outstanding were to be withdrawn from circulation (the operation to be completed by

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<sup>a</sup> The monetary convention of 1857 provided for the introduction into the Austrian monarchy of the 45-florin standard. A pound (500 grams) of pure silver was to be coined into 45 florins. This new florin was henceforth the standard monetary unit. The ratio between the old "convention" coin and the new coin was such that 100 florins of the former was equal to 105 florins of the latter.

October 31, 1859). The volume of the 5, 2, and 1 florin convention-coin notes was to be reduced as rapidly as practicable to the aggregate of 100,000,000 florins.<sup>a</sup> A further step toward the establishment of the Austrian standard was the issue of the imperial ordinance of December 26, 1858, decreeing the complete withdrawal from circulation of these small notes by December 31, 1859. The National Bank was authorized to issue in their place 1-florin notes (Austrian standard) up to the amount of 100,000,000 florins. The Government agreed at the same time to diminish its indebtedness to the bank by turning over to it 30,000,000 florins (Austrian standard), which money the State was to receive in installments (in coin) in 1860-1864 as the purchase price of the South Austrian-Italian Railway, and by handing over to it in addition government debentures to the amount of 23,000,000 florins, secured by obligations on the part of landowners released from feudal payments to the State.

Whether the resources at the command of the bank at that time were sufficient for maintaining the redeemability of the notes could not be determined, inasmuch as the redemption had to be suspended on April 29, 1859, owing to the war in Italy. The imperial decree of that date provided for the making of a very considerable loan by the bank to the Government, which was to make an issue of 5 per cent bonds to the amount of 200,000,000 florins. (Austrian standard). As this issue could not be floated at the time, the minister of finance was authorized to borrow from the bank (according to the needs of the imperial exchequer) on the security of the bonds, taken

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<sup>a</sup> The paper money of the "Viennese standard" had ceased to be legal currency on July 1, 1858.

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at two-thirds of their nominal value. The bank was at the same time authorized for this purpose to issue 5-florin notes, Austrian standard, which were to be a legal tender. In accordance with this arrangement the Government borrowed from the bank in the course of the year 1859 the sum of 133,000,000 florins, and, in addition, 20,000,000 florins in coin. The unfortunate outcome of the war prevented the immediate repayment of these sums.

In the period 1847-1859, the National Bank established 19 branches in the provincial capitals and in Hungary. The economic conditions enabled the bank to continue enlarging its discount business down to 1857. The loan business expanded rapidly until at the close of 1857 the loans amounted to 86,000,000 florins. Much favoritism was shown in the granting of credit. The rate of discount (and the rate of interest on loans) was raised in 1856 from 4 per cent (which it had been since 1833) to 5 per cent. The annual sum paid out as dividends increased from 1853 to 1858, but, owing to the increase of the capital stock, the annual dividends per share decreased from 85 florins (convention coin) in 1854 to 60.57 florins (Austrian standard) in 1858.

### V.—THE THIRD CHARTER OF THE NATIONAL BANK (1862).

The Government did not hesitate, immediately after the conclusion of peace, to resume the work of placing the monetary system of the country on a sound basis. The first matter to be dealt with was the indebtedness of the State to the National Bank. By virtue of an agreement of April 1, 1860, the Government turned over to the bank securities from the sinking fund that had been abolished at the close of 1859 to an amount which reduced

the recently contracted debt (the interest on which was 2 per cent) from 133,000,000 florins to 99,000,000 florins. The issue of the loan of 200,000,000 florins, for which provision had been made in 1859, was ordered in March, 1860. It was to be in the form of an interest-bearing debt repayable with prizes (the so-called "1860 drawings"). The 123,000,000 florins of bonds that remained unissued out of the 200,000,000 florins was handed over to the bank as security for the debt of 99,000,000 florins. The installation in 1861 of a national parliament (*Reichsrath*), consisting of a chamber of deputies (the members of which were elected by the provincial diets) and of an upper house (House of Lords) created a new authority to deal with the monetary situation. After protracted parliamentary discussions the law of December, 1862, was enacted, providing for a new agreement with the National Bank regarding the extension of its charter, new statutes, and a readjustment of the indebtedness of the State to the bank. The new statutes went into effect on January 6, 1863.

The term of the new charter of the National Bank was to extend to the close of 1876. It was provided that the total indebtedness of the Government to the bank should be discharged by the close of 1866, with the exception of the sum of 80,000,000 florins, which was to continue as a loan until the expiration of the new charter.<sup>a</sup> The bank was

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<sup>a</sup> The indebtedness of the Government to the bank on November 29, 1862, was as follows: 36,900,000 fl. on account of the redemption of the so-called "Viennese currency;" the 20,000,000 fl. in silver borrowed from the bank in 1859; a debt of 77,800,000 fl. (the remnant of the debt of 133,000,000 fl. contracted in 1859), secured by the government debentures of 1860; and a debt of 87,000,000 fl., secured by imperial domains. The repayment was to be effected in part by cash payments in installments, in part through the proceeds of the loan of 1860, and in part by means of the revenues from the imperial domains and of the sums realized from the sale of such lands.

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to resume specie (silver) payments in 1867. The committee of one hundred was to be replaced by a general assembly of the shareholders owning individually at least 20 shares. The general assembly was to choose from its midst 14 "directors" (the choice to be subject to the confirmation of the Emperor) who were to serve for three years. These directors, with the governor, were to constitute the board of managers. The general assembly was moreover to choose from its midst a committee of 12 members (the term of service being one year), who were to have a voice in the deliberations relative to changes in the rate of interest. The reports of the directors regarding the management of the institution and those of the committee regarding the statements were to be submitted to the general assembly for its approval. The governor was to be appointed by the Emperor and the two vice-governors were to be chosen by the directors from their midst for a term of three years. The capital stock of the bank was fixed at 110,250,000 florins.

The bank was to have the exclusive privilege of issuing "drafts on itself," noninterest-bearing and payable to the bearer on demand. The smallest denomination of these bank notes was to be 10 florins, but the 1-florin and 5-florin notes outstanding were not to be withdrawn from circulation until legal provision was made for the purpose. The obligation was imposed on the bank of redeeming its notes at their face value in legal silver coin, but this provision was declared to be in abeyance for the time being. The circulation in excess of 200,000,000 florins must be covered by the full amount of silver (gold might be substituted for silver up to one-fourth). The circulation in

excess of the metallic reserve was to be covered by discounted bills or securities furnished as collateral, negotiable debentures of the bank, etc. The notes were to be a legal tender throughout the entire extent of the monarchy, with the exception of the Lombardo-Venetian Kingdom. The bank was to publish monthly statements. The provisions regarding the relations with the Government were completely changed. The control exercised by the State was henceforth to be restricted to a supervision of the management of the bank by a commissary, with reference to a due observance of the statutes and *règlement*. The business between the Government and the bank was to be confined to the discounting of bills presented by the minister of finance and to transactions executed by the bank on commission.

It appeared certain down to April, 1866, that if nothing interfered with the carrying out of the agreement of 1862, the resumption of specie payments in the year 1867 might be accomplished. At the close of 1866 the bank-note circulation was estimated at 298,000,000 florins, against which there was a metallic reserve of 148,200,000 florins. Conformably to the provision in the charter regarding reserve against circulation, this left a note reserve of 50,200,000 florins. The prospect of resumption in 1867 was, however, dispelled by the issue of irredeemable legal-tender paper currency by the Government in 1866 for the expenses of the war against Prussia and Italy—paper money that was kept in circulation after the close of the war. The law of May 5, 1866, declared the 1-florin and 5-florin bank notes a legal tender government currency and relieved the National Bank from the obligation of redeeming them in

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silver. The maximum volume of such notes was fixed at 150,000,000 florins. It was provided that the bank should furnish the Government, on account of the notes thus taken over, an equivalent amount of bank notes of larger denominations. By the law of July 7, 1866, the minister of finance was authorized to borrow 200,000,000 florins, and the National Bank was charged, until the conditions should admit of the floating of a loan or the issue of regular government currency, to advance provisionally the requisite funds in bank notes up to the sum of 60,000,000 florins, it being provided that the sums thus advanced should be repaid in bank notes within a year after the conclusion of peace. The law of August 25, 1866, provided for a further increase in the paper currency of the Government and at the same time for a limitation of the total circulation. The minister of finance was instructed to make a fresh issue of 90,000,000 florins in 1-florin and 5-florin government notes and an additional issue of 60,000,000 florins, which should enable it to repay the National Bank for its advances. The aggregate of the government paper currency was thus increased to 300,000,000 florins, and it was provided that this sum should not be exceeded.<sup>a</sup> The government notes were declared a legal tender. The 60,000,000 florins was repaid to the National Bank in 1867, so that the indebtedness of the State to the bank was restored to the former figure of 80,000,000 florins. In order to pay the war indemnity to

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<sup>a</sup> Except in so far as it was provided that in case the total volume of treasury bills secured by a mortgage on the imperial salt works (*Salinen-scheine*) should sink below the maximum of 100,000,000 florins, the difference should be made up by an additional issue of government notes. The departure from the maximum limit down to the redemption operations of 1894 did not exceed 12,000,000 florins.

Prussia, the metallic reserve of the bank had to be temporarily appropriated by the Government. A syndicate of financiers obtained from the bank through the channel of discounts the sum of 30,000,000 florins in silver, which was lent to the Government and which was promptly repaid.<sup>a</sup>

This issue of government paper currency assailed the chartered privileges of the bank and was a menace to its business, the injury to which was soon apparent in a decline in the volume of commercial discounts for many months together, due no doubt to the increased circulation of the new notes. In 1867 the National Bank was unable for the first time since 1819 to pay its shareholders a dividend of 7 per cent. It had recourse to a provision in the agreement of 1862 by which the Government bound itself on account of the loan of 80,000,000 florins (the remnant of its indebtedness to the bank), the term of which was to extend to the expiration of the new charter, in case the dividends in any year should sink below 7 per cent, to make up the deficiency in whole, or in the event of its exceeding 1,000,000 florins, in part up to that sum.<sup>b</sup> The bank naturally put forward a claim for indemnity, and secured from the Government a modification of the statutes such as was calculated to insure an increase in its earnings. The act of October 13, 1868, reduced the capital stock to 90,000,000 florins, and the quota that was to go to the sur-

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<sup>a</sup> The premium on silver florins, which, from 1862 to February, 1866, had declined from 38.67 to 1.75 per cent, rose again in the latter year to 29.75. The averages for the years 1867-1873 were 23.95, 14.43, 21.02, 21.89, 20.38, 9.27, 8.14.

<sup>b</sup> The Government paid the sum demanded, but when, in 1868, the dividends were again below 7 per cent the complementary payment was not made. The result was a lawsuit which was terminated in 1878 by an agreement in which the bank withdrew its claim.

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plus from 25 to 10 per cent, and authorized the bank to take deposits on certificate with or without the payment of interest and to allow interest in connection with accounts current. The loan business was extended (Hungarian securities being now included in the admissible collateral) and more scope was given to discount transactions and the commission business. The discount business expanded steadily from 1868 to 1873 as a result of the great economic development that was manifesting itself in Austria. Under these conditions the bank was obliged to mobilize its resources and to take every precaution to insure the required metallic reserve against a large note circulation.

In the years 1871 and 1872 the National Bank converted a considerable part of its metallic reserve from silver to gold, a step which was of great moment with respect to the monetary standard of the country. At the close of 1869 the gold holdings of the bank amounted to 20,435,000 florins (all but 235,000 florins being in the shape of foreign bills) and the silver holdings (*Vereinstaler*, Prussian talers, Austrian florins, bullion, etc.) to 126,900,000 florins. At the close of 1872 the figures for the gold had grown to 74,100,000 florins (only 4,600,000 florins being foreign bills), while those for the silver had declined to 83,500,000 florins. In order to permit of this change, which was effected quietly without any disturbance of the money market, the provision in the bank statutes according to which the substitution of gold for silver in the metallic reserve was restricted to one-fourth of the total had to be rescinded (act of March 18, 1872). The union of the two halves of the Austro-Hungarian monarchy in the matter of customs and commerce consummated by

the agreement of December 24, 1867, contemplated the speedy introduction of the gold standard according to the principles laid down at the Paris monetary conference, and the act of March 9, 1870, had decreed the coinage of gold pieces of 8 and 4 florins (equivalent to 20 and 10 francs), it being provided that the exchange value of these coins should be left to the determination of the market until the introduction of the gold standard.<sup>a</sup> It was not this, however, that compelled the action of the bank management in changing from silver to gold. It was determined, rather, by the pessimistic view (which proved to be well-justified) entertained by the managers regarding the future of silver. It was the intention of the secretary-general of the bank to convert the entire metallic reserve of the bank from silver into gold, but the decline in the price of silver forced a suspension of such operations in 1875.

The industrial and commercial expansion in Austria that had set in in 1868 brought on a great crash at the Bourse in May, 1873, which precipitated an economic crisis. The demands upon the bank had been steadily increasing, and on May 13, 1873, with notes outstanding to the amount of 329,800,000 florins, its reserve was only 13,300,000 florins. The fact that the bank was unable, with due observance of its statutes, to grant any further credit, even to individuals whose credit was the best and who offered the safest securities as collateral, would have sufficed to destroy public confidence, already so badly shattered. In order to avert such a catastrophe the Government found itself constrained to suspend by

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<sup>a</sup> It was not until 1892 that provision was made for the establishment of the gold standard by the parliaments of the dual monarchy.

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an imperial decree the provision of the statutes regarding the metallic reserve against circulation. This ordinance remained in force until October, 1874.

In the following years of economic depression the discounts of the bank decreased from 181,700,000 florins at the close of 1873 to 117,100,000 florins at the close of 1875. The dividends increased steadily from 1869 to 1873, owing to the increasing demands of the business world which the bank was called upon to meet, until they exceeded 11 per cent. After that there was a drop, the dividends for 1875 being  $8\frac{1}{3}$  per cent.

### VI.—THE NATIONAL BANK IN ITS RELATIONS TO HUNGARY, 1867–1878.—TRANSFORMATION OF THE NATIONAL BANK INTO THE AUSTRO-HUNGARIAN BANK.

In the year 1867 the so-called *Ausgleich* was concluded between Austria and the lands of the Hungarian Crown, changing fundamentally the parliamentary régime inaugurated in 1861. As under the new order the system of coinage and the monetary unit were to be adjusted on the same basis in the two halves of the monarchy, it was provided that the Austrian standard, until the law regarding it was changed, should remain the common standard. The debt represented by the government notes was placed under the joint guaranty of the Austrian and Hungarian governments. The system of banks of issue was not embraced in the matters that were to be adjusted according to identical principles in the two halves of the monarchy. The provisions of the agreement between Austria and Hungary made no mention

of the bank notes that were in circulation by the side of the government notes and were invested with the same privileges, or of the charter of the National Bank, which had been granted with reference to the entire monarchy for a term extending to the close of 1876, or of Hungary's share in the debt of 80,000,000 florins to the bank. Some understanding in regard to these matters had, however, to be arrived at, and, as a matter of fact, the bank was at the time the subject of agreements between the Austrian and Hungarian governments, as it afterwards developed. In an arrangement concluded between the ministries of the two halves of the monarchy on September 12, 1867, the Hungarian ministry assumed the obligation, so long as no legal provisions regarding banks and paper money were enacted by mutual agreement for the monarchy as a whole, not to allow any bank of issue in Hungary, and to permit the notes of the National Bank to remain a legal tender in the kingdom (receivable for all dues to the Government), a necessary condition being that the National Bank be bound to establish branches in Hungary wherever the Government should deem it necessary, and to grant loans on the securities of both halves of the monarchy. This agreement was not formally communicated to the bank until the beginning of 1870.

This arrangement led to an ever-increasing complication of the bank question, and it was not until May, 1876, that the two governments could come to a definite understanding regarding the basis of a settlement. It was agreed that the issue of bank notes should be assigned by the two governments as an exclusive privilege to a

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single banking corporation, which should establish two banking institutions, having equal privileges, at Vienna and at Budapest, and in whose central governing body the two halves of the monarchy should be equally represented. Of the legally permissible note issue, 70 per cent was to be assigned to the institution at Vienna and 30 per cent to the one at Budapest. This scheme was embodied in the legislation of 1878. The National Bank was transformed into the Austro-Hungarian Bank and the term of the new charter was to extend from July 1, 1878, to the close of 1887, for which period the two governments renounced the privilege of creating independent banks of issue. The matter of the debt of 80,000,000 florins was adjusted at the same time.

The central managing body of the Austro-Hungarian Bank, styled the general council, was to consist of the governor, appointed by the Emperor upon the joint nomination of the Austrian and Hungarian ministers of finance, an Austrian and a Hungarian vice-governor, appointed by the Emperor from a list submitted by the general assembly of the shareholders, and twelve councilors. The councilors were to be chosen by the general assembly—two from a list of candidates submitted by the directorate at Vienna, two from a list submitted by the directorate at Budapest, and eight from the midst of the assembly itself. Their nomination was to be subject to the Emperor's confirmation. The directorates, or managing boards of the institutions at Vienna and Budapest, were to consist of eight members, and were to be presided over by the Austrian and Hungarian vice-governors, respectively. Two of the directors were in each case to be the councilors

chosen by the general assembly from the aforesaid list and the remaining six were to be named by the general council. Supervision over the entire management of the bank was to be exercised by the secretary-general. The parity of the two halves of the monarchy was to be evidenced, among other things, by the bilingual character of the bank notes. The notes of the Government were to be included in the nonmetallic reserve against circulation. Interest was not to be allowed on money deposited on certificate. It was provided that the redemption of the bank notes should be suspended until the time when the government notes were deprived of their legal-tender quality. A feature of the new charter was the participation of the two governments in the profits of the bank. In the first place such a fraction of the net annual profits was to be distributed among the shareholders as amounted to 5 per cent of the paid-in capital; 10 per cent of the remainder was to be assigned to the surplus; so much of what was left was to go to the shareholders as was required to make the annual dividends equal to 7 per cent of the paid-in capital; of what remained after that one-half was to be turned over to the shareholders and one-half to the two governments in the proportion of 70 per cent for Austria and 30 per cent for Hungary. The profits of the two governments during the continuance of the charter were to be devoted to the diminution of the debt of 80,000,000 florins to the bank, which during this period was not to bear any interest. Hungary was to pay Austria after the expiration of the charter an amount equal to 30 per cent of what remained of this indebtedness (in 50 annual installments). While the legislation of 1878 placed the two halves of the monarchy on an ostensible

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parity as regards the share of influence in the management of the bank, no provision was in reality made to establish actual parity with respect to the general council, eight of the twelve members of which the general assembly was allowed to choose from among its own members, irrespective of whether they were Austrian or Hungarian citizens. It was to be expected that the choice would fall upon Austrian citizens, which would mean an Austrian majority in the general council. And so it came to pass, parity being therefore not realized to this extent. This arrangement, by which the ultimate composition of the general council was left to the shareholders, although at variance with the original standpoint of the two governments, worked perfectly well. The statutes in which it was embodied existed for more than twenty years, to the satisfaction even of the Hungarians, who are extremely sensitive with respect to such matters.

In the period of the first charter of the Austro-Hungarian Bank (1878-1887) its holdings of silver increased from about 70,000,000 florins to 145,000,000 florins. This was due to the fact that, owing to the fall in the price of the metal (after 1873),<sup>a</sup> arbitrageurs set to work (from 1876 on) to import it into Austria-Hungary in order to have it converted into coin, an importation which assumed very large dimensions, especially in the years 1878 and 1879. The bank was obliged by its statutes to pay on demand 45 florins in bank notes for a pound of pure silver.

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<sup>a</sup> The premium on silver florins (taking the average for the year) in the five years 1874-1878, was as follows:  $5\frac{1}{4}$ ,  $3\frac{2}{5}$ ,  $4\frac{3}{5}$ ,  $9\frac{2}{5}$ , and  $3\frac{1}{5}$  per cent. It disappeared at the close of 1878. The price of gold, as expressed in Austrian paper money did not, of course, partake of this movement.

From the year 1876 the bank declined to abide by this provision on the ground of the inability of the mint at Vienna to undertake the coinage. The statutes of 1878 provided that the obligation to buy should last only so long as the coinage of silver on private account was not suspended. Its suspension was decreed in March, 1879. The governments of Austria and Hungary continued, however, to coin silver, and so the volume of silver florins went on increasing from year to year, and as they were not in demand in business they kept pouring into the vaults of the bank. In spite of the efforts made to get rid of them by selling at favorable moments the stock grew larger and larger, the increase continuing after 1887.

#### VII.—THE SECOND CHARTER OF THE AUSTRO-HUNGARIAN BANK (1887).

By the legislation of May, 1887, the charter of the Austro-Hungarian Bank was renewed for a term of ten years. During the period of the first charter it became evident that the maximum volume of notes unsecured by a metallic reserve that the bank was permitted by its statutes to issue—200,000,000 florins—was insufficient. Its discount business increased greatly from 1880 to 1884, and the newly established branches brought a large increase in the volume of its transactions, so that at times the institution was barely able to meet the demands for credit made upon it. The management petitioned to have the provision regarding the metallic reserve amended and to have the system intro-

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duced that obtained in the case of the German Reichsbank.<sup>a</sup> The new statutes provided that if the circulation exceeded the metallic reserve (in which foreign bills up to 30,000,000 florins might be included) by more than 200,000,000 florins, the bank was to pay a tax of 5 per cent on the excess, of which tax 70 per cent was to go to the Austrian Government and 30 per cent to the Hungarian.<sup>b</sup> The total circulation was to be secured by a reserve of silver or gold of not less than two-fifths and by readily convertible securities for the remainder.<sup>c</sup> The statutes of 1887 paved the way for a great development of the giro business<sup>d</sup> of the Austro-Hungarian Bank.

### VIII.—INTRODUCTION OF THE GOLD STANDARD IN AUSTRIA-HUNGARY.

The measures instituted by the governments of Austria and Hungary for the introduction of the gold standard inaugurated the great period in the history of the Austro-Hungarian Bank. The fixing of the coinage system and of the monetary unit was, according to the spirit of the agreement of 1867, establishing the relations between the two governments, a matter to be dealt with according to identical principles in the two halves of the monarchy.

<sup>a</sup> The system which allows an unsecured note circulation up to a prescribed maximum, which may be exceeded on the condition of the payment of a tax on the excess.—TRANSLATOR.

<sup>b</sup> The proceeds of the tax were to be applied to the liquidation of the 80,000,000 fl. debt to the bank.

<sup>c</sup> Deposits repayable on demand were likewise to be covered by securities.

<sup>d</sup> The system which provides for the method of payment by means of transfers to and deductions from accounts current.—TRANSLATOR.

By the legislation of 1892<sup>a</sup> the governments of Austria and Hungary substituted for the Austrian standard (so called) the gold standard, the monetary unit of which was to be the crown.

As the introduction of the new standard could be consummated only after the lapse of a considerable interval of time, no change was ordained for the time being in the valence of the various kinds of money of the Austrian standard, and it was provided that the new coins should be a legal tender in the case of all obligations in which payment in the Austrian standard was contracted for and, *vice versa*, the florin being reckoned equal to two crowns. The enforced universal adoption of the crown standard in connection with the reconstitution of the coinage system as a whole, the disposition to be made of the coins of the Austrian standard of the two halves of the monarchy, the redemption of the government notes, the adjustment of the paper currency, and the instituting of specie payments were to be provided for by special legislation. In accordance with the new standard 1 kilogram of pure gold was to be coined into 3,280 crowns. The current coins were to be 20-crown and 10-crown pieces;<sup>b</sup> as one florin was made

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<sup>a</sup> By the side of the laws enacted a treaty making those laws mutually binding was concluded between the two governments on August 11, 1892. It placed the coins that were to issue from the mints of the two governments on a perfect equality in either half of the monarchy in all private transactions as well as in payments into the public treasuries. The cost of redeeming the coins of the Austrian standard and of the government paper currency was to be borne by the governments of Austria and Hungary in the ratio of 70 per cent and 30 per cent. The terms of the treaty were to remain in effect until 1910, or, if neither party gave notice of withdrawal, until 1920.

<sup>b</sup>A 100-crown piece was added in 1907

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equal to two crowns, the relative values of gold and silver according to which the transition from the Austrian to the gold standard was effected were in the ratio of 1 to 18.22. The value of the crown as expressed in the franc, the mark, and the English penny is approximately 1.05, .85, and .99. The crown was divided into 100 hellers. There were to be bronze coins of 1 and 2 hellers, nickel coins of 10 and 20 hellers, and silver pieces of 1 crown. From 1899 there were also silver pieces of 5 crowns. The coinage of the silver money of the Austrian standard of the separate halves of the monarchy, as well as of the gold pieces of 8 and 4 florins (trade coins, 42 gold florins equal to 100 crowns), was to be discontinued. The coins of the Austrian and of the "convention" standard have ceased to be current coin long ago with the exception of the silver florin piece, which continues to be regular money, equivalent to 2 crowns. The date fixed for the introduction of the gold standard as the legal standard was January 1, 1900.

The reform of the monetary standard brought in its train important changes in the Austro-Hungarian Bank. It was provided that the bank should be obliged to buy on demand at its main establishments legal gold coins (at their nominal value) and gold bullion in accordance with the monetary unit of the crown standard, with the deduction of the seigniorage fixed by the laws of the two governments—6 crowns per kilogram of pure gold in the case of private individuals and 4 crowns in that of the Austro-Hungarian Bank. The bank published a schedule of the rates governing the purchase of foreign coins and of trade

coins.<sup>a</sup> The acquisition of gold was facilitated by the reduction in 1903 of the seigniorage in the case of coinage for the bank to 2 crowns. As a rule, the Austro-Hungarian Bank pays the highest rate after the Bank of Russia. By utilizing the means afforded it—taking advantage of times when the state of foreign exchange favored such operations and often making advances without charging interest to the importers of gold—the bank has been able to lay in a large stock of gold in the course of years.<sup>b</sup> The bank obligated itself in 1892 not to buy silver bullion without the sanction of the two governments. In the absence of a legally established or prescribed ratio, the bank had been appraising its stock of gold in florins of the Austrian standard according to the gold-silver ratio of 1 to  $15\frac{1}{2}$ . But in 1892, when a legal basis for the valuation was afforded, it made a new appraisement in accordance with the ratio of 1 to 18.22. As against the book valuation of 79,392,613 florins, there was a resultant gain of 13,525,167 florins, by way of exchange, which sum the bank incorporated in its surplus, carrying over to it a like amount of foreign bills taken out of the stock reckoned as part of the metallic reserve.<sup>c</sup>

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<sup>a</sup> From 1902 the management of the bank was authorized to raise or lower the schedule figures for certain specified kinds of coin within certain limits, so as to be in a position, according to the state of the money market or the market for foreign bills, to encourage the inflow of the kinds of coin most in demand and hinder the importation of the kinds not easily absorbed by the market. It soon raised the price of the French coins in denominations of francs, so useful in the settlement of international obligations on the part of the monarchy, and later it lowered the price of the eagle.

<sup>b</sup> The purchases of the bank in the years 1892-1907 aggregated 647,500,000 crowns.

<sup>c</sup> This amount of foreign bills was consequently no longer available as a cover for note circulation.

## IX.—THE REDEMPTION OF THE GOVERNMENT PAPER CURRENCY.

Soon after the enactment of the laws that were to pave the way for the introduction of the gold standard the Austro-Hungarian Bank was called upon to cooperate in the redemption of the notes of the Government. This was accomplished by means of two successive operations. The legislation of 1894 (in Austria and Hungary) provided for the redemption of 200,000,000 fl., and the redemption of the remainder was decreed by an imperial ordinance in 1899. In the first operation all the 1-florin notes were called in and as much of the 5-florin and 50-florin notes as made up the sum of 200,000,000 fl. Up to the sum of 40,000,000 fl. the notes were replaced by silver coin of the denomination of 1 crown, the material for which was lying in the treasuries of the two governments in the shape of superannuated coins, "union" dollars (*Vereinstaler*), "convention" coins, etc. The remaining 159,328,000 florins<sup>a</sup> were replaced up to the sum of 38,841,300 florins by silver florins which the two governments obtained from the bank; and for the rest (120,486,700 florins) by notes likewise furnished by the bank, which received from the two governments the equivalent in 20-crown gold pieces. The governments supplied the necessary gold out of the proceeds of loans (gold rentes), which they had been empowered to issue by the legislation of 1892, and out of the stocks in their treasuries. It was provided that the bank should use the gold received in exchange for its notes only as a reserve

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<sup>a</sup> One-florin notes to the number of 672,000 were not presented for payment.

against these notes. The 1-florin notes had to be presented for redemption before the close of 1899. By the close of 1897 the 5-florin and 50-florin notes were redeemed up to the requisite figure. In pursuance of an imperial decree issued in 1899 the redemption of 112,000,000 florins was undertaken. They were replaced by 5-florin pieces up to the sum of 32,000,000 florins, and for the remainder (80,000,000 florins), by notes of the Austro-Hungarian Bank of the denomination of 10 crowns. The bank furnished the silver to the two ministries of finance in the shape of florin pieces and received from them 112,000,000 florins in 20-crown gold pieces, of which 80,000,000 florins (160,000,000 crowns) was to be set aside as a reserve against the bank notes. The gold had been all transferred to the bank by August, 1901. The government currency was redeemed at the bank. What still remained of government paper money (11,312,000 florins) had been substituted for treasury bills based on the security of the government salt works (*Partial-Hypothekaranweisungen*, popularly known as *Salinen-scheine*) and the cost of its redemption had to be borne by the Austrian Government exclusively. The Austrian ministry of finance redeemed this paper in 1899-1900, issuing in place of it treasury bills of the kind here described. The obligation to accept government notes in payment of debts terminated in 1903.

The withdrawal of the government paper currency from circulation was a measure eminently calculated to bring the problem of the gold cover for the bank notes nearer to a solution. The bank received in all from the two governments in the above-mentioned transactions 542,600,000 crowns in gold coin. At the close of 1899 the

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Austrian Government paid the bank in addition 30,000,000 florins in the new gold coins on account of the so-called 80,000,000-florin debt, the bank agreeing in consideration of this payment to scale down the debt to 30,000,000 florins, charging its surplus fund with the amount thus deducted (28,291,000 crowns). The metallic reserve was further strengthened by the transfer to it from the surplus of 15,000,000 fl. in foreign bills in connection with the enlargement of the capital stock of the bank on the occasion of the renewal of its charter in 1899. Thus the tax-free circulation might be increased by 90,000,000 crowns.

### X.—RENEWAL OF THE BANK CHARTER IN 1899.

The charter of the Austro-Hungarian Bank was renewed in 1899 (by legislation in Hungary and by imperial decree in Austria) for a term extending to the close of 1910 (or, under certain conditions, to the close of 1907). The term of the charter had expired in 1897, but its provisions had twice been declared to remain in force for another year.<sup>a</sup> The statutes were amended in important respects and the modifications expressed the full recognition of the claims of Hungary. The parity of the two halves of the monarchy with respect to the bank was secured by various innovations. It was provided that six of the twelve members of the general council elected by the shareholders must be Austrian citizens and six Hungarian. The general council was to consist of the governor, the twelve elective

<sup>a</sup> The *Ausgleich* ("settlement") between Austria and Hungary was extended in 1899 until the close of 1907. The main subjects of the so-called "economic settlement" were those relating to customs and trade, the participation of the two governments in the common expenditures of the monarchy, and the system of bank-note circulation. In 1907 the *Ausgleich* was extended until 1917.

members, the Austrian vice-governor and his deputy, and the Hungarian vice-governor and his deputy. The executive committee and the committees of the general council chosen to deal with the various branches of business were to be composed equally of Austrian and Hungarian citizens. The meetings of the executive committee and of the other committees were to be held at Vienna and Budapest (according to the instructions of the governor) and, as far as practicable, alternately at the two cities. The meetings of the general assembly of the shareholders were to be held at Vienna or Budapest according as to whether the majority were Austrian or Hungarian citizens. Owing to the greatly superior number of the Austrian shareholders, this provision has instituted no practical change.

The governmental control over the management of the bank was extended in various ways. The number of representatives of the two governments in the general council was increased by the addition of the two deputy vice-governors. The vice-governors were henceforth to be appointed by the Emperor not from a list submitted by the general council but on the nomination of the respective ministers of finance. It was provided that the resolutions of the general council, the executive committee, and the various standing committees of the general council must receive the approval of the governor in order to become effective, and that in like manner the resolutions of the two directorates (at Vienna and Budapest) must be submitted to the presiding officer, that is to say, the vice-governor or his deputy. The two government commissioners were

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empowered to take part in the deliberations of the executive committee and the standing committees. It was made the duty of each of these commissaries to protest against any resolutions of the general assembly of the shareholders, the general council, the executive committee, a standing committee of the general council, or the directorate that he might consider opposed to the interests of that part of the monarchy which he represented. They were to be permitted to acquaint themselves with the details of the management of the bank. In case of a protest the matter was to be left to the decision of the common ministry. The new statutes provided that the governor, the vice-governors, and the deputy vice-governors should be appointed for a term of five years only. They might, however, be reappointed.

The ministers of finance of Austria and Hungary, in an identical note addressed to the Austro-Hungarian Bank under date of August 1, 1894, had expressed the desire that the bank, in order to further the reform of the monetary standard, should extend as far as possible its dealings in foreign bills and all kinds of metallic currency. The statutes were remodeled so as to provide for the bank a broader legal basis for its activity in this direction. The institution was authorized to open interest-bearing accounts so as to enable it in case of need to draw money from abroad by the payment of interest in place of putting up the rate of discount. One of the provisions of the new statutes imposed upon the bank the obligation to receive moneys for account of the two fiscal administrations and to make payments for account of either up to the amount of its credit balance. The bank had repeatedly

represented to the two governments the desirability of having the free cash of the central government treasuries transferred to its vaults in order that it might exercise a greater influence on the domestic money market. The new arrangement contemplated the simplification of the business of the government treasuries by the exploitation of banking facilities in the matter of payments. A large number of the government treasuries have linked themselves to the giro system of the Austro-Hungarian Bank as well as to that of the postal savings banks. The proper policy would be to place all the disposable government moneys in the hands of the bank in order to afford it the means of exerting that influence which it is absolutely necessary that it should have with respect to the money market and the rate of discount. One of the functions with which the bank was invested was that of effecting the gold transactions of the governments of the two halves of the monarchy, as well as those of the common authorities, a matter that was of great importance with respect to the conduct of its foreign-bill business. The bank was obliged by the new statutes to attend to the money-changing business of the two ministries of finance and to perform this task gratuitously, it being part of the "regulation of the monetary circulation," which is designated in article 1 of the statutes as the duty of the bank. The bank is obliged to place at the disposal of the business community the kinds of money that it asks for and to try to remove, as far as it is practicable, interlocal differences in value.

## *The Austro-Hungarian Bank*

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In the readjustment of the matters pertaining to the monetary standard and the Austro-Hungarian Bank in 1899, it was assumed that the reform of the monetary standard through the initiation of the compulsory redemption of the notes of the bank would probably be consummated in the course of the term of the bank's charter, and regard was had for this in the drafting of the provisions relative to the denominations of the bank notes. It was provided that the lowest denomination should be 50 crowns in place of the previous 10 crowns. The reason assigned for this new restriction was that business would not need any small notes as soon as it was possible to reckon on a sufficient supply of coin, and that the unrestricted issue of small notes would drive coin from circulation. The bank was permitted to issue 20-crown notes, but only during the interval until the instituting of specie payments, it being provided, moreover, that the volume of such notes should be fixed at any time by the ministers of finance of the joint governments. As a matter of fact, the issue of 10-crown notes was provided for, but this was done by the enactment of a special law, so that the bank could be obliged at any time to withdraw these notes partially or entirely on the demand of the joint governments, made with the sanction of the two parliaments. The bank notes were to retain the legal-tender quality. According to the former statutes, the obligation of the bank to redeem its notes was to remain in abeyance so long as the government notes were not divested of their legal-tender quality in both halves of the monarchy. According to the new statutes, this obligation was not to ensue of itself

on the abolition of the legal-tender quality of the government notes, but it was provided that as soon as these notes ceased to be a legal tender the two parliaments might decree that article 83 of the statutes should go into effect.

The sphere of activity of the two directorates was extended. The Austrian and Hungarian directorates were to consist, respectively, of the Austrian and Hungarian vice-governor and deputy vice-governor and of the Austrian and Hungarian members of the general council. To each of the directorates was to be attached a "central inspector" appointed by the general council, who was to be a member of the "management."<sup>a</sup>

The new arrangements relative to the participation of the State in the profits of the bank were less favorable to the institution than the previous ones. Out of the net annual earnings a sum was first of all to be distributed among the shareholders equal to 4 per cent of the paid-in capital; <sup>b</sup> after that 10 per cent of the net earnings was to be allotted to the surplus and 2 per cent to the pension fund; of the remainder, in so far as the total dividends did not exceed 6 per cent of the paid-in capital, one-half was to be assigned to the shareholders and one-half to the joint governments; of what remained after that, one-third was to be distributed in dividends to the shareholders and two-thirds were to go to the two governments. The share of the State in the profits was no longer to be divided between Austria and Hungary in the ratio of 70 to 30. This division was at first too favorable to Hun-

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<sup>a</sup> The advisory council of the secretary general of the bank, consisting of the chief officials.

<sup>b</sup> This was raised by the new statutes from 90,000,000 fl. to 105,000,000 fl.

## *The Austro-Hungarian Bank*

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gary, but the situation had changed, inasmuch as in the ten years, 1888-1897, 36½ per cent of the earnings of the bank subject to tax had come from its Hungarian business. The Hungarian Government made it a condition of its entering into negotiations regarding the renewal of the bank charter that its share of the profits should be proportioned to the earnings of the bank in the Hungarian half of the monarchy.

It was provided that the joint governments should have the right (the sanction of the two parliaments having been previously obtained), on the expiration of the term of the bank's charter, or in the event of the dissolution of the corporation prior to the expiration of the charter, to take over the whole banking concern that constituted the object of the charter (with the exception of the mortgage department, which was to be left to the company) in the shape and form in which it existed on the balance sheet and according to the valuation expressed by the balance sheet. The shareholders were to receive 1,520 crowns for each share and, in addition, the amount of the surplus. This joint right of acquisition was, however, not to be regarded as involving an agreement between the two governments for the preservation of a single bank of issue for the two halves of the monarchy. The term of the new charter was made to date from January 1, 1900, and its duration was to extend (with reference to the duration of the agreement between the two governments relative to the coinage and the monetary standard) to the close of 1910. It was provided that in case the duration of the customs union of the two halves of the monarchy was not prolonged by the legislatures beyond the

close of 1910, the term of the charter was to expire at the close of 1907.

## XI.—DEALINGS OF THE AUSTRO-HUNGARIAN BANK IN FOREIGN BILLS AND FOREIGN METALLIC CURRENCY.—THE PLACING OF THE MONETARY SYSTEM OF AUSTRIA-HUNGARY ON A SPECIE BASIS.

The Austro-Hungarian Bank has, since 1896 and more especially since 1901, expanded the volume of its dealings in foreign bills and all kinds of metallic currency to vast dimensions, a policy closely connected with the reform of the monetary standard. The activity of the bank in this direction is directed toward the steadyng of the foreign exchanges and the maintenance of the relative values of the crown (the unit of the Austro-Hungarian gold standard) and the standard gold coins of other countries, as established in 1892. It is universally admitted that the bank has developed its foreign exchange and foreign coin business along model lines with the achievement of the complete control of the market, and it has done this, not for the sake of profit, but solely in the interest of the public. The maintenance of a rate of exchange as close as possible to parity is rightly considered as a matter to be dealt with by the national administration and as a function appertaining to the central bank of issue, which is not supposed to act in this capacity as an institution organized for profit, but as an organ of the Government instituted for the purpose in question, and which, it is presumed, will be ready to incur losses should circumstances demand it. With reference to the object aimed at, it was of the utmost importance that the joint

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governments should lodge their gold with the bank and assign to it the task of effecting their gold transactions. The specie paid into the government treasuries had previously been deposited with private bankers, who allowed a low rate of interest and who bound themselves to furnish the sums needed for the foreign payments of the governments at particular dates in the kinds of coin required up to the amount of the credit balances. This led to periodical excessive rises in the exchanges, perhaps often artificially induced, which were detrimental with respect to fiscal conditions and the monetary standard. The banks, besides, made use of the government funds in international speculations. In order to remedy this unsatisfactory state of things, the two ministers of finance entered in 1901 into an agreement with the Austro-Hungarian Bank by which they contracted to hand over to it in future the gold that came into the government treasuries and to effect their international payments through its channels. The bank contracted in return to pay interest on the deposits and to administer the funds—not merely by making payments for account of the governments directly out of the money deposited, but also by purchasing with its notes foreign metallic currency whenever commissioned to do so—and bound itself, furthermore, although as yet no laws had been enacted providing for compulsory specie payments, to get gold into circulation. This agreement was ratified by the common ministry of the monarchy.

As early as August, 1901, the bank began to take steps to get the Austrian and Hungarian gold coins into circulation, and it has continued to discharge this function ever

since, paying out gold and redeeming bank notes in gold on demand. As international settlements are effected by means of gold payments, the action of the bank meant practically the inauguration of specie payments. By the close of 1906 gold coin of the two governments to the amount of 1,250,000,000 crowns had been paid out, only one-fourth of which remained in the hands of the public. The remainder was neither hoarded up nor exported, but found its way back to the bank in a perfectly normal manner, just like bank notes, by means of payments or through the process of exchange. Professor von Bilinski, governor of the Austro-Hungarian Bank, remarked in his interesting lecture on "International Payments" (1906): "The fact that in the course of five years a whole billion in gold in full-weight coins could be kept in the country and returned to the vaults of the bank instead of being used in international payments is perhaps the best evidence of the effectiveness of the bank's activities in the very domain of such payments."

Having assumed the function of effecting for the State all payments that were required to be made in gold, the Austro-Hungarian Bank organized its foreign-bill department in such a way as to be able to serve the Government on the one hand and on the other to meet the legitimate needs of the public with respect to the international market by enabling it at all times to buy and sell foreign bills of exchange and coin of all nations on the most favorable terms. "Its action in either direction must, however, be so exerted," says Bilinski, "that the metallic stock of the bank shall remain as far as possible undisturbed. Foreign bills are to be used to the greatest prac-

ticable extent in international payments, and compensatory payments from abroad are to be made to take place as often as possible, so that, in spite of all the efflux and reflux in international payments, any unfavorable change in the value of the standard coin of the country relatively to foreign money (in other words, a premium on foreign coin), bringing with it a rise in the rate of discount, may be averted. The performance of such a task demands a widely ramified activity. While permanently maintaining assured credit balances at all the more important banks and banking houses all over the world, the bank must make it its constant and daily concern to manage its foreign-bill business in such a way as to make it conform to the needs of the existing situation. In accordance with the state of the market and the quotations for metallic currency, as well as the needs of the public, the bank either buys foreign bills, paying with its own notes or with checks drawn against credit balances abroad, or else it sells foreign bills, receiving in exchange its own notes or foreign checks, or, in certain cases, foreign bank notes and foreign gold." The total volume of transactions in the department of foreign bills in a single day has reached the sum of 71,900,000 crowns. In the conduct of that part of its business which consists in the purchase and sale of foreign bills and metallic currency the element of profit has not been permitted to be more than an ulterior object in the policy of the Austro-Hungarian Bank. The main thing held in view has been to guard the monetary standard of the monarchy. The excellent results of the policy pursued by the bank in its dealings in foreign bills have been clearly indicated by the course of exchange. After

the high premium of the years 1893 and 1894, the foreign exchanges since 1896 have been very satisfactory. In the years 1901-1906 the average rate of exchange (taking each year by itself) did not fluctuate up or down by more than one-fifth of 1 per cent, and the average deviation from parity during any one month did not exceed three-tenths of 1 per cent. In the year 1907, when an extraordinary stringency prevailed in the monetary market, the maximum premium on bills drawn on London, Paris, and Berlin was, respectively, .97, .79, and .24 per cent. This result is all the more satisfactory in that the bank's rate of discount in that year was on an average only 4.9 per cent, being finally put up in November from 5 to 6 per cent.<sup>a</sup>

In 1903 the governments of Austria and Hungary submitted to their respective parliaments a bill providing for the inauguration in the near future of the compulsory redemption of bank notes. It soon became evident that there was very little chance of its being enacted into a law at an early date as the Lower House of the Hungarian Diet was at the time involved in a critical situation by reason of the Nationalist demands with respect to the common army. The partisans of national independence adopted a policy of obstruction, and there was no prospect of permanently normal parliamentary activity on the part of the Hungarian Lower House for years to come. A serious and protracted political crisis ensued. The Liberal party, which had constituted the majority in the Lower House ever since 1867, was beaten in the elections in January, 1905, and for a considerable time there was no parliamentary ministry.

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<sup>a</sup> The rate was therefore considerably below that of the German Reichsbank.

## The Austro-Hungarian Bank

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It was not until April, 1906, that a ministry was installed representing the great majority of the members of the house. The new Hungarian Government had, however, much weightier cares than the redemption of the bank notes in specie,<sup>a</sup> for the *Ausgleich* between the two halves of the monarchy was to expire at the close of 1907, and it was necessary to make a new arrangement. An agreement between the two governments was arrived at in October, 1907, providing for the renewal of the customs union for a period of ten years. Usually the question of the bank was settled simultaneously with the main matters involved in the *Ausgleich*, but on this occasion such settlement was not imperative, inasmuch as the charter of the bank, in consequence of the legislative enactment relative to the customs union, could remain in force till the close of 1910.<sup>b</sup> It would have been a good thing if a decision had been reached to renew the charter of the bank, but it happened otherwise. It is certain that a considerable section of the Hungarian Parliament was, at that time, at least, not desirous of such a solution. A separate bank of issue was as much a part of the programme of the party of independence as the separation from Austria in the matter of customs. A compromise was finally effected, by which the bank question was to remain for a time in abeyance, a parliamentary committee being appointed to undertake a preliminary discussion of the matter.

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<sup>a</sup> The bill submitted to the Austrian Parliament was withdrawn on July 7, 1906.

<sup>b</sup> According to the provisions regarding the bank which went into operation on January 1, 1900, its charter was to expire at the close of 1907 in case the customs union was not extended beyond the close of 1910.—TRANSLATOR.

# National Monetary Commission

## XII.—STATISTICAL TABLES.

### *Business of the Austro-Hungarian Bank since 1880.*

[In millions of crowns.]

At the end of—	Capital.	Dis- counts.	Loans.	Note cir- culation.	Depos- its.	Metallic cash.	Divi- dends for the year.
							Per cent.
1880—	180.0	278.2	41.8	657.2	10.4	346.6	6.38
1885—	180.0	272.8	54.4	727.2	5.3	397.4	6.45
1890—	180.0	333.2	82.6	891.8	13.0	439.0	7.88
1895—	180.0	438.8	92.4	1,239.6	25.2	741.2	7.36
1900—	210.0	455.5	67.1	1,494.0	48.7	2,158.0	5.69
1905—	210.0	641.2	68.2	1,846.9	160.6	1,365.0	5.01
1906—	210.0	770.9	98.9	1,982.0	205.4	1,394.3	6.45
1907—	210.0	748.0	125.3	2,028.0	151.7	1,380.8	7.67

<sup>a</sup> From 1900 the fractional currency of the crown standard is included in the metallic cash.

### *The discount business.*

[Aggregate of discounts in each year in millions of crowns.]

Year.	Number of offices in Aus- tria.	Number of offices in Hun- gary.	Total number of offices.	Aggregate of dis- counts at the Austrian offices.	Aggregate of dis- counts at the Hungarian offices.	Aggregate of dis- counts at all the offices.
1880—	28	22	50	992.6	324.8	1,317.4
1890—	98	82	180	1,324.4	555.0	1,879.4
1900—	100	103	203	1,889.8	1,008.8	2,898.6
1907—	122	132	254	3,494.8	2,243.1	5,737.9

# The Austro-Hungarian Bank

Note reserve and excess circulation.

Year.	Reserve of circulation not subject to tax (in millions of crowns).	Circulation subject to tax (in millions of crowns). <sup>a</sup>				Amount of tax paid on circulation during the year (in crowns).
		End of year.	End of September.	End of October.	End of November.	
1888	25.4					
1889	24.0					
1890	15.0			46.4		99,304
1891		11.6		23.8		91,570
1892	37.4					
1893	31.8			13.4		33,390
1894	14.5			4.0		4,258
1895			13.4	75.9	21.2	392,858
1896				14.4		48,636
1897	12.7					
1898		16.0		80.4	18.0	429,366
1899		19.4		28.2		162,250
1900	55.5					
1901	233.5					
1902	225.2					
1903	88.6					
1904	135.5					
1905				7.3		33,812
1906		45.5	130.8	19.7	130.2	470,634
1907		167.1	242.1	98.4	187.1	1,886,460

<sup>a</sup> Prior to 1907 the only months in which there was a circulation subject to tax were September, October, November, and December. In that year there was an excess circulation in March, June, July, and August (as much as 92,500,000 crowns in the last-named month).

## Metallic cash of the bank.

[In millions of crowns.]

At the end of—	Gold.	Silver.	At the end of—	Gold.	Silver.
1880	130.0	216.4	1900	919.6	238.5
1890	108.0	330.8	1901	1,116.1	271.9
1895	488.0	253.2	1905	1,074.1	290.9
1897	727.4	246.6	1907	1,099.3	281.4

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## Rates of exchange for bills drawn on Berlin, Paris, and London.

[The average per cent for each year is given. Above par is indicated by +; below par by -.]

Year.	Berlin.	Paris.	London.
1892--	-5	-0.5	-0.6
1893--	+3.2	+3.2	+3.1
1894--	+4	+4.1	+3.8
1895--	+1.4	+1.5	+1.5
1896--	+0.1	+0.2	+0.1
1897--	-0.1	-0.1	-0.4
1898--	+0.1	-0.1	+0.2
1899--	+0.3	+0.4	+0.4
1900--	+0.6	+1.1	+0.8
1901--	-0.2	+0.1	-0.2
1902--	-0.3	+0.1	-0.2
1903--	-0.3	0	-0.3
1904--	-0.3	0	-0.2
1905--	-0.17	+0.23	-0.04
1906--	-0.15	+0.30	+0.09
1907--	+0.02	+0.44	+0.31

## The rate of discount.

Year.	Lowest rate.	Highest rate.	Year.	Lowest rate.	Highest rate.
1886--	4	4	1897--	4	4
1887--	4	4½	1898--	4	5
1888--	4	4½	1899--	4½	6
1889--	4	5	1900--	4½	5½
1890--	4	5½	1901--	4	4½
1891--	4	5½	1902--	3½	4
1892--	4	5	1903--	3½	3½
1893--	4	5	1904--	3½	3½
1894--	4	5	1905--	3½	4½
1895--	4	5	1906--	4	4½
1896--	4	5	1907--	4½	6

## Development of the giro business of the bank.

Year.	Crowns.	Year.	Crowns.
1887--	1,634,000,000	1900--	24,517,000,000
1890--	8,953,000,000	1907--	63,626,000,000

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# The Banking System of Japan

BY

**MARQUIS KATSURA**

Premier and Finance Minister of Japan

**BARON SAKATANI**

Ex-Minister of Finance

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Financier

and

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# THE BANKING SYSTEM OF JAPAN.

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## I.

BY

MARQUIS KATSURA.

*Premier and Finance Minister of Japan.*

The introduction of the new régime, following the restoration of the Throne to the actual rulership of Japan, in 1868, ushered in an era of extensive development and advance in various branches of industry. National finance formed no exception; indeed it exhibited remarkable progress. But to place the entire system of national finance on a sound basis involved great difficulties and was necessarily a gradual process, each phase requiring its full period of evolution.

## HISTORY OF THE JAPANESE BANKING SYSTEM.

During the early portion of the Meiji era (dating from A. D. 1868) the financial system of Japan was primitive, and, as it then existed, was local and limited. The amount of capital was insufficient, and the rate of interest constantly rising. Private loans were hampered, and the balance of trade was always unfavorable. After the establishment of the national banks and of the Specie Bank some improvement was made in the finan-

cial system of the country, but this was only a beginning when judged by a national standard. The improvements and developments were along collateral lines, and with the growth of the branches the necessity of a trunk powerful and strong enough to support them came to be felt. In other words, there arose an urgent demand for the establishment of a great central banking institution. We shall now proceed to give more fully the reasons for the establishment of the Central Bank in Japan.

The banking business in Japan dates from the eleventh month of the fifth year of Meiji (1872). (The Gregorian calendar came into use the following year.) The bank regulations were promulgated at that time, and in August of the ninth year (1876) amendments were introduced to those regulations and the number of banks increased to over 150. During the first ten years, however, the banks suffered from the disadvantages of small capital and lack of cooperative facilities.

As a remedy for some of the existing evils, public opinion rapidly crystallized in favor of a Central Bank which might bring about fuller cooperation among the financial institutions by securing control of the essential machinery of the national finance. By establishing a Central Bank, it was expected that the evils of the financial system in vogue, which might be termed the feudal system, would be obviated, and it was also hoped that by converting the national banks into agencies or branches of the central banking institution, having a complete system of communication, an even operation would be attained, and the working of the entire machinery facilitated throughout the whole Empire. It was further

## *The Banking System of Japan*

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believed that the small banks would come to rely upon the Central Bank and realize the advantage of cooperation with it.

The capital of most of the banks in those days was very limited, and they were totally unable to cope with any sudden demand for large amounts of money. When, on the occasion of a flurry in the money market, the demand for the discounting of bills assumed unusual proportions, or when deposits were extensively withdrawn, suspension of payment was not infrequent. Credit consequently was impaired, or at least was uncertain, the result being that money was kept in private hands. Under such conditions no financial system could be expected to work smoothly. As long as this state of things prevailed it was impossible to inspire confidence or to draw out into circulation the volume of money individually hoarded.

It was expected that with the establishment of a Central Bank, empowered to make adequate advances, the danger of a serious crisis or panic following financial stress would be averted, and the development and advancement of commercial interests, which would attract increased capital, would be amply provided for. It was believed that as a result of the aid extended by the Central Bank to the smaller banks the suspension of industrial or commercial development on account of lack of necessary capital would be avoided.

In early days in Japan the issue and volume of currency, when compared with the standard of living and the state of commerce and industry, were rather excessive, but the circulation of that currency was far from being uniform and ample. The rate of interest was ever on the

increase, due to the withdrawal of capital from circulation and the fact that the banks were advancing large sums on long-term loans. But, with a Central Bank exclusively engaged in discounting bills and in making advances for short periods on the best bills, capital would be active and interest low. Such an institution would, in fact, regulate the rate of discount and largely that of interest.

In European countries the Government extends protection and assistance to a Central Bank, and government money is deposited in that bank, which devotes the surplus standing to the Government's credit to the purchasing of foreign drafts or bullion. No effort is spared looking to the importation of specie.

In Japan also it was seen that, should a Central Bank be firmly established, the monetary transactions of the Treasury and the redemption of government bonds would be transferred to such a bank, and any surplus would be devoted to the purchase of national and foreign coins and bullion, which would be ultimately employed in converting the government notes. This accomplished, a way would surely be opened for concentrating specie, and, eventually, notes would be placed on a convertible basis. The money paid locally in the form of taxes being mostly brought to the Central Government, leaving only such a portion of it as was required for local governmental expenses and other small items, a deficiency in circulating currency was felt severely each year at the tax-paying period, and the interest on money always rose. But it was felt that if the monetary transactions of the Treasury should be intrusted to a Central Bank

## *The Banking System of Japan*

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the volume of currency temporarily in the one bank would be more speedily reduced by the discounting of bills and other processes, and the money market would be relieved promptly. Thus it was expected that the bank's operations would be adjusted to the actual needs of the market.

Financial troubles in those days were generally attributable to the outflow of gold abroad, caused by the unfavorable state of the balance of foreign trade. But the experience of excess of imports over exports is not limited to Japan. There are times when European countries have a like experience, and the reason why, in those countries, the deficiency of specie is not severely felt, even under an unfavorable balance, may be found in the fact that there exists a financial institution for importing specie from abroad. Japan, in those days, had no such institution. There was an exit for specie, but no inlet for it; in other words, foreign goods were paid for in Japanese specie alone, and no other means were available for making the payment. It was realized that the establishment of a Central Bank would open the way for bringing in foreign money. In Europe the banks, by holding correspondence with other banks, are in close touch as to the volume of specie in different countries and are constantly adjusting the balance by rate of discount. Such work can be undertaken only by a central banking institution, and such a bank once established, a financial organ would be brought into existence which could maintain a constant watch on the financial and commercial conditions of the world, and would be able on the one hand to help smaller banks, and on the other to open a gate for the incoming of

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foreign specie, so that, even in case of import exceeding export, causing the outflow of specie, no apprehension need be entertained.

### **WHY THE BELGIAN SYSTEM WAS ADOPTED IN JAPAN.**

After careful study and comparison of the central banking systems of Europe we found that, although in extent of business, power, and influence in the financial world the Bank of France and the Bank of England were unrivaled institutions, yet in point of perfection of organization the Bank of Belgium was peerless. With the exception of the Imperial Bank of Germany, the Bank of Belgium is the most modern creation. It was organized after careful comparison of the banking systems of England, France, Austria, America, and other countries, and the best in all those systems was adopted, while the weak points were carefully avoided; consequently it was decided by Japan to adopt the Belgian system.

The Imperial Bank of Germany, being an institution adapted to the needs of a federation of States, was found unsuitable for Japanese purposes, while the Bank of England and the Bank of France had all the characteristics born of long usages and history, and consequently it was not possible to adopt their system in a country like Japan where no similar conditions exist.

Though the Belgian system was adopted, yet in note-issuing capacity and the rate of reserve a method resembling the German one was included.

# *The Banking System of Japan*

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## THE BANKING SYSTEM IN GENERAL AND WHY THE SYSTEM WAS ADOPTED.

With the establishment of the Meiji Government, one of the policies followed was to perfect as far as possible the financial system of the country and to promote and encourage production throughout the Empire.

As early as the first year of Meiji (1868) a commercial office was established with the object of encouraging commercial and industrial development. The organization of the office was afterwards placed on a more efficient basis. Under its jurisdiction were placed the mercantile companies and the exchanges, which were the banks in those days. These exchanges (*Kwase*) were the first real bankers in this country. The capital was supplied by wealthy merchants by subscription, while the Government also advanced funds. The exchange received deposits, advanced loans, and issued drafts. It was also authorized to issue notes against the reserves.

The object sought in the establishment of these exchanges was good, but their organization and regulations were very defective, and moreover they constituted an identification, or at least a combination, of the Government with private interests. Therefore the system was soon found to be unsuitable at a time when the country was undergoing a rapid transformation on account of the new régime; and after several failures among the exchanges, hope of success was abandoned, and, in about 1870, the Government realized the necessity of establishing a more perfect system.

In the fifth year of Meiji (1872) the regulations for national banks were promulgated. The American system

had been adopted, and in March of the following year the regulations for national bonds convertible into gold were enacted. With the establishment of the national bank system the exchanges were dissolved, except one in Yokohama, which was allowed to continue business after having been converted into a national bank; thus was the Second National Bank established. This bank, besides the privilege of issuing ordinary notes, was clothed with authority to issue foreign silver notes, which, however, was forfeited when the Bank of Japan was established and issued convertible notes.

Four banks were established at the time of the promulgation of the banking regulations of 1872, the First National Bank being one. The amount of capital was 3,450,000 yen, with right to issue notes to the extent of 2,070,000 yen.

The volume of inconveritible government notes steadily increased, specie began to command a premium, and showed a tendency to leave the country. In those days bank notes were immediately brought to the issuing bank for conversion, and there was no prospect of a smooth or general circulation of the notes issued by the banks. Consequently the note-issuing privilege granted to the banks proved useless; indeed it constituted a detriment to the business of banking. Thus the first object of the Government in promulgating the banking regulations, namely the adjustment of the inconveritible notes, failed utterly.

In 1876 the Government introduced important amendments in the banking regulations, and, instead of requiring the conversion of the bank notes into gold, made it possible

## *The Banking System of Japan*

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to convert them with currency. In other words, the banks could convert their notes with those of the Government, and the result was the introduction of inconvertible notes. The banks were also authorized to deposit eight-tenths of their capital in the form of government bonds valued at the market price and to issue notes equal to the amount of their deposits, while the remaining two-tenths of the capital was to be reserved in the form of currency to meet the demand for conversion. These amendments proved to be of great advantage, and the number of banks suddenly increased to 152, representing capital of 42,110,000 yen, the notes issued reaching the sum of 34,390,000 yen.

The Satsuma rebellion of 1877 caused the Government to increase the issue of its inconvertible notes, and the new notes thus emitted amounted to over 27,000,000 yen. Besides, the Government also issued reserve notes to the amount of over 20,000,000 yen. The bank notes, as already stated, also increased, and reached the amount of over 34,000,000 yen. The total of inconvertible notes rose to 160,000,000 yen. Specie began to command a premium, and with the depreciation of the value of the notes, uneasiness spread on every side. It was immediately and plainly apparent that there was an urgent necessity for changing this state of affairs by a reform of the note-issuing system. This brought about the introduction of further fundamental reforms in the banking system of Japan.

With the increase in the volume of the bank notes the Government became apprehensive and saw the necessity for limiting the right of establishing banks. In 1877 the bank regulations underwent fresh amendment. The

Minister of Finance was invested with authority to place restrictions on the establishment of banks, to limit the amount of capital, and to lower the note-issuing capacity. This was followed by the policy of redeeming the inconvertible notes, which was consistently carried out, nor were the bank notes left unredeemed.

In 1883 the bank regulations were again amended, and a clause was introduced whereby it was made impossible for a bank to continue as a national bank after the term of its charter expired, and it was also provided that no bank should have power to issue notes. Simultaneously measures were taken whereby the bank notes should be redeemed gradually. With the expiration of the terms of charter of the national banks an attempt was made to have the charters made renewable, but, this proving futile, the national banks very smoothly changed into private banks, so that by February, 1899, the former completely went out of existence. The disappearance of the national banks, however, did not mean complete withdrawal from circulation of the notes issued by them, but by placing a limit on the period of their circulation they were completely withdrawn by December, 1904, after which the government and bank notes ceased to circulate, and the unification of the paper currency was thus effected.

#### THE YOKOHAMA SPECIE BANK.

The Yokohama Specie Bank was established in 1880, and the Bank of Japan came into existence in 1882. The former was organized on the joint-stock principle for the purpose of facilitating foreign trade and also of issuing convertible notes as the circulation of specie increased.

## *The Banking System of Japan*

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But as the notes showed signs of depreciating, the note-issuing license was not granted to the Specie Bank. From the time of its establishment the Specie Bank was devoted to foreign exchange and issuing drafts on commercial commodities. The history of the Bank has not been untroubled, but with foresight as to developments it increased its capital in 1887 to 6,000,000 yen. The Government extended special protection to the Bank under its Yokohama Specie Bank regulations, and since that time the Bank made steady progress and developed without a hitch, until by 1896 its capital was doubled and became 12,000,000 yen. With this increase of its capital, necessity was felt for extending the sphere of its operations, and this called for further increase of its capital by 2,000,000 yen, making a total of 14,000,000 yen. The business of the Bank is now in a thriving condition.

The present regulations for the Yokohama Specie Bank limit its business to the following:

- (1) Foreign exchange and issuing of drafts on commercial commodities.
- (2) Inland exchange and issuing of drafts on commercial commodities.
- (3) Advancing loans.
- (4) Deposits of money and custody of articles of value.
- (5) Discount and collection of bills of exchange, promissory notes, and other securities.
- (6) Exchange of coins.

### THE BANK OF JAPAN.

The Bank of Japan is organized and modeled after the Central Bank of Belgium. The purpose of the Bank was to withdraw inconvertible notes from circulation, thereby

unifying the paper currency of the country; to facilitate the handling and disposition of money belonging to the Treasury and of the National Bonds; to adjust the monetary conditions prevailing at home and abroad, and regulate the rate of interest. The Bank was established in 1882 by virtue of Imperial Ordinance No. 32. Its authorized capital now stands at 30,000,000 yen and it is privileged to issue convertible bank notes. The maximum of the notes to be issued against the reserve was at first 70,000,000 yen, which was afterwards increased to 85,000,000 yen, and is now further increased to 120,000,000. The governor and vice-governor are appointed by the Government. The Bank is placed under several restrictions. The Government reserves the right to attach supervising officials, thus bringing the institution under the strictest governmental surveillance.

As already stated, the first Exchange Company ended in failure, while the national banks did not achieve what had been expected of them. The amendments to the bank regulations resulted in the increase of inconvertible notes, and this called for further amendments of the regulations. The Yokohama Specie Bank was confronted with difficulties almost immediately after its establishment, so that, in view of the existing financial condition of the country, the establishment of the Bank of Japan was epoch making: it not only placed the fiscal policy of the Government on an entirely new footing, but it also exercised a wholesome and beneficial influence on the economics and finance of the entire country.

## *The Banking System of Japan*

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The business now transacted by the Bank of Japan is as follows:

- (1) To discount or purchase government bills, bills of exchange, and commercial bills.
- (2) To buy or sell gold or silver bullion.
- (3) To make loans on security of gold and silver coins and bullion.
- (4) To collect bills for banks, companies, and merchants who are its regular customers.
- (5) To receive deposits in current account and to accept the custody of articles of value, such as gold, silver, and precious metals, and documents.
- (6) To make advances in current accounts or loans for fixed period on security of government bonds, treasury bills, and other bonds and shares guaranteed by the Government. The amount of such loans and the rate of interest are to be decided from time to time by the conference of governors, vice-governors, directors, and supervisors, subject to the approval of the Minister of Finance.

The Bank of Japan, besides engaging in the above-stated business, is disqualified from engaging in the following transactions:

- (1) Making loans on the security of real estate or shares of banks or corporations.
- (2) Making loans on the security of shares of the Bank of Japan, or purchasing the same.
- (3) Becoming a shareholder of industrial corporations, or engaging, either directly or indirectly, in industrial enterprises of any kind.
- (4) Becoming the owner of real estate, except so far as is necessary for establishing the head office and branches of the bank.

In 1890 ordinary bank regulations were enacted by Law No. 72, which was followed by savings banks regulations Law No. 73. The promulgation of these regulations opened a new epoch in the history of banking in Japan. By the new regulations the banking business was clearly defined, and all those engaged in that and similar business were brought under special contract by those regulations. Before the law came into force there existed no instrument for the control of private banks. Only special institutions, such as the Bank of Japan, the Yokohama Specie Bank, and national banks, were under the control of the Government. When the national banks became private banks, after the expiration of their charters, they passed out of the control of the Government. The new regulations changed all this.

The necessity of creating a banking center in order to facilitate the management of national finance, and the importance of government control and supervision and of insuring a wholesome development, were what led to the new regulations; for it was feared that the national banks which were formerly under government control and supervision would, when they passed beyond that supervision, prove obstacles to such development.

#### THE SAVINGS BANKS.

The savings bank, above all other banks, requires most careful supervision by the Government. In Japan the Government has a Postal Savings department and also a deposit section in the Department of Finance. But the amount of the deposit being found too small when compared with the population and the standard of eco-

## *The Banking System of Japan*

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nomics in general, the Government enacted a new regulation for savings banks, with a view to increasing the amount of the deposit by initiating a method for supervising, controlling, and improving the business of the private institutions. According to these regulations, banks that receive deposits at compound interest are classed as savings banks, and their organization must be on the joint-stock principle. It is also made obligatory on such banks to keep a reserve as security for repayment amounting to not less than one-quarter of the whole amount of the deposit, in the form of interest-bearing national or local bonds, and to have them deposited in the place authorized to receive them. In other respects the provisions of the ordinary bank regulations apply to the savings banks.

In 1896 the Hypothec Bank of Japan was created by Law No. 82, and in the same year the Agricultural and Industrial Bank was also established under the Law No. 83. These laws opened another epoch in the history of Japanese banking. The banks so far were engaged in making loans and receiving deposits for short terms, and also in discounting commercial bills, so that they were principally organs for commercial transactions. But the credit system not being fully developed in the country, the need was strongly felt of an institution where long-term loans could be obtained on security of movable and immovable property. Such loans being incompatible with the practical working of ordinary banks, difficulties were experienced in some cases.

Of recent years, however, the commercial credit system having considerably developed and the necessity being felt of establishing a special institution for making long-term

loans for the benefit of agricultural and industrial interests, the Government made the necessary investigations to meet this requirement. Then the war with China broke out, with the result that a very large sum of money was scattered among the people. On the other hand, the post-bellum measures called for a large amount of capital to be devoted to unproductive works, and it was thought most timely and necessary to open a way for absorbing small funds widely distributed throughout the country, and devote them to developing agricultural and industrial interests. With this object, the Hypothec Bank and the Agricultural and Industrial Bank were organized and established by the law issued in 1895.

The Hypothec Bank of Japan, created by the law relating thereto, has for its object the advancing of funds for the purpose of improving and developing agricultural and industrial enterprises, and the Bank is organized on joint-stock principles, with the president and vice-president appointed by the Government. Its principal business is to advance loans on mortgage of immovable property which shall be redeemable by annual installments, the Bank being placed under severe restrictions in other lines of business. It is authorized to issue mortgage debentures bearing premiums to an amount not exceeding ten times its paid-up capital, provided the amount of such debentures does not exceed the total amount of outstanding loans redeemable by annual installments. The Bank enjoys a government subsidy to the extent of guaranteeing 5 per cent dividend for ten years after its establishment, in case its profits fail to realize that standard of dividend.

## *The Banking System of Japan*

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The Agricultural and Industrial Bank is a joint stock company established in every prefecture. These banks have for their object the advancing of loans for the purpose of improving and developing agricultural and industrial interests. Their business is similar to that of the Hypothec Bank, only on a small scale. The banks are also placed under the same restrictions and government supervision as the Hypothec Bank. They are authorized to issue agricultural and industrial debentures to an amount not exceeding five times the paid-up capital. The Government delivered a sum of about 10,000,000 yen to the prefectoral authorities for taking up the shares of the agricultural and industrial banks of their localities, and on this amount the Bank is exempted from paying a dividend.

The two banks above described being exclusively engaged in making long-term loans on the security of immoveable property, the need arose for a financial organ which could advance long-term loans on the security of government bonds, shares, and movable property. It was also deemed advisable to combine in such an organ the business of a trust company. The institution born of these requirements is the Industrial Bank of Japan, organized under the law relating thereto and enacted in March, 1900, as Law No. 70.

The Industrial Bank is a joint stock company, and the governor and deputy governor are appointed by the Government. The capital of the Bank is 17,500,000 yen, and foreigners own no small portion of the shares. It acts as a medium for the introduction of foreign capital, and is thus engaged in adjusting and facilitating circulation of capital at home and abroad. The Bank is

authorized to issue debentures to an amount not exceeding ten times its paid-up capital, provided the amount of such debentures does not exceed the total amount of outstanding loans and negotiable instruments actually in hand.

The Bank has a government subsidy to the extent of guaranteeing a 5 per cent dividend for five years after its establishment in case its profit fails to come up to that dividend.

#### THE BANK OF FORMOSA.

The Bank of Taiwan (or Formosa) was established under the law relating thereto and promulgated in 1900 as Law No. 38. The Bank is a private stock company with a capital of 5,000,000 yen, and its president is appointed by the Government. It is placed under several restrictions, and the Government exercises strict supervision over the management. The privileges granted to the Bank consist in the Government taking up 1,000,000 yen of its capital, for which no dividend is claimed for five years; in the authorization to issue notes against the guaranteed reserve to the amount of 5,000,000 yen free of tax, and in the loan from the Government of 2,000,000 yen without interest for five years, to be used as a reserve against the issuing of notes. The purpose of the establishment of the Bank was to reform the currency system of Formosa, to facilitate the receipts and disbursements of the Treasury, to develop the working of the process of exchange, and to facilitate the investment and subscription for the Formosa public-works bonds.

In the colonial policy of Japan the adjustment of finance is of prime importance, and it was at first thought that it could be carried out by intrusting the work to the Bank of

## *The Banking System of Japan*

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Japan or to the Yokohama Specie Bank, but Formosa being a new territory, where special conditions prevail, it was thought better to establish a special institution. The result was the establishment of the Bank of Taiwan.

### THE HOKKAIDO COLONIAL BANK.

The Hokkaido Colonial Bank was established as a joint-stock company, with a capital of 5,000,000 yen, in 1899. The Government has an official attached to the Bank, and exercises strict supervision. The object of the Bank is to supply the capital necessary for colonizing and developing the Hokkaido, by making long-term loans on the security of immovable property, payable in annual installments. It can also make other loans and issue drafts on commercial commodities. The Hokkaido being still undeveloped in agriculture and other industries, and being subject to conditions different from other parts of the Empire, it had been deemed necessary to establish this bank in place of the Agricultural and Industrial Bank, in order to meet the special requirements of the island.

The system and working of different kinds of banks in Japan, and the reasons for their adoption, are as briefly stated above. The table on page 140 shows the number, the amount of capital, etc., of these banks. It is based on actual conditions prevailing in December, 1907.

# National Monetary Commission

Kinds of bank.	Authorized capital.	Capital paid up.	Reserve.	Number of offices.		When established.
				Head.	Branch.	
Bank of Japan	Yen. 30,000,000	Yen. 30,000,000	Yen. 21,500,000	1		8 October, 1882.
Yokohama Specie Bank	24,000,000	24,000,000	14,591,707	1		24 February, 1880.
Hypothee Bank of Japan	10,000,000	4,250,000	1,503,481	1		0 June, 1897.
Agricultural and Industrial Bank	29,320,000	28,620,000	4,596,310	46		1 November, 1897. <sup>a</sup>
Bank of Taiwan or Formosa	5,000,000	3,500,000	830,000	1		1 August, 1900. <sup>b</sup>
Hokkaido Colonial Bank	5,000,000	3,750,000	381,000	1		9 June, 1899.
Industrial Bank of Japan	17,500,000	16,250,000	623,200	1		5 March, 1900.
Ordinary banks	416,687,230	291,599,745	84,182,982	1,058		1 February, 1902.
Savings banks	69,688,600	42,234,296	-----	484		162 March, 1876. <sup>a</sup>
Same, combining ordinary banking	6,595,000	5,285,719	11,421,423	192		711 281
Total	607,195,830	444,204,041	139,630,103	2,194		921

<sup>a</sup> Earliest estimated.

<sup>b</sup> Latest.

# THE BANKING SYSTEM OF JAPAN.

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## II.

### OPINIONS OF BARON SAKATANI,

*Ex-Minister of Finance.*

The banking system in Japan was at first modeled after the national-bank system of the United States. The banking regulations promulgated in 1872 closely followed the American system, being almost a translation into Japanese of the American regulations. As it was found, however, that such a system did not work well on account of its being unsuitable to national conditions, the regulations were amended in 1876 and in 1882, when the central bank system was adopted. The Bank of Japan was then established, and the national banks, at the expiration of their charter of twenty years, were not allowed to exist as national banks, but such as wished to carry on a banking business became ordinary banks.

In 1890 the regulations for ordinary banks and savings banks were promulgated, but the Bank of Japan, the Yokohama Specie Bank, the Hypothec Bank, the Agricultural and Industrial Banks, the Industrial Bank of Japan, the Bank of Formosa, and the Hokkaido Colonial Bank are placed under special laws, enacted to meet their respective requirements.

The Bank of Japan is modeled after the Central Bank of Belgium; the regulations concerning the issue of convertible notes were, however, copied from the German system in order to secure sufficient elasticity in operation.

## *National Monetary Commission*

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### RELATIONS OF THE BANK OF JAPAN TO OTHER BANKS.

The relations of the Government to the ordinary banks are very simple. The Government for the purpose of protecting the interests of the creditors exercises supervision over the business of those banks. It is within the province of the Minister of Finance to give official recognition to their establishment and to inspect at any time the actual state of the banks' business. The banks are also obliged to publish periodical balance sheets.

The relations between the Government and the Bank of Japan are of a very close character. When the latter was first established, the Government was a very large shareholder, but these shares were afterwards transferred to the Imperial Household Department. The Bank of Japan is responsible for the custody of the Government's cash and negotiable instruments. It is intrusted with the management of the treasury receipts and disbursements; the investment of the treasury funds and the management of national bonds are also committed to the Bank of Japan. In this respect the Bank is almost a part of the Department of Finance, and performs valuable services in simplifying and facilitating the work of that department. In consideration of the privilege of being intrusted with the receipts and disbursements of the Treasury the Bank is obliged to transact that business without remuneration, except in special instances. The business of the Bank of Japan is placed under well defined limitations by law, in order to insure the stability of its business and also to prevent the misuse of its influence. The Government's supervision is very strict. It appoints the

## *The Banking System of Japan*

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governor and the deputy governor; the directors are also appointed by the Government from among candidates elected by the shareholders; the Government appoints official inspectors from among the officials of the Department of Finance, these official inspectors having a voice in the directors' meetings and also in the meetings of the shareholders, but they have no vote in either of those meetings.

The Bank of Japan has the privilege of issuing convertible notes. This is considered its most important function. The mode of issuing such notes and the duty to be paid thereon are governed by very strict laws.

### THE YOKOHAMA SPECIE BANK.

The Yokohama Specie Bank was established largely through the influence of Count Okuma, then Minister of Finance. Japan's national finances were at that time in a very bad state. The inconvertible government notes had depreciated, and specie was withdrawn from the market. In order to remedy this condition of the money market a bank for transacting business in specie was established, so as to absorb the specie of the country. But the attempt being fundamentally erroneous, and its method of operation faulty, the Specie Bank suffered great loss and was reduced to very sore straits. Afterwards, however, great improvements were introduced in the Bank's business methods by the efforts of Count Matsukata, Minister of Finance, and since that time the Bank has recovered from the losses then sustained and is at present in a prosperous state.

The directors of the Yokohama Specie Bank are elected by the shareholders and are subject to approval by the Government, which appoints official inspectors for the Bank's business. The Government was at first a large shareholder, but its shares have since been transferred to the Imperial Household Department.

The Yokohama Specie Bank has very close relations with the Bank of Japan, the latter exercising strict supervision over the business of the former. Under the law the deputy governor of the Bank of Japan acts as governor of the Yokohama Specie Bank, and the deputy governor of the latter acts as director of the Bank of Japan.

The Yokohama Specie Bank is an organ of foreign exchange established to foster foreign trade and to absorb specie from abroad. For that purpose the Bank of Japan advances funds to the Yokohama Specie Bank at a specially low rate, and also rediscounts bills at the request of the Specie Bank. The Bank of Japan never engages directly in foreign exchange or in sending money abroad. Government bonds abroad and receipts and disbursements of the treasury funds abroad are managed by the Yokohama Specie Bank under the supervision of the Bank of Japan. Such funds of the latter as are kept abroad are placed under the management of the Specie Bank. It is not privileged to issue notes at home, but its agencies in China and Manchuria are authorized by the Japanese Government to issue silver notes payable on demand.

The entire banking system of Japan centers in the Bank of Japan, with ordinary banks and savings banks,

## *The Banking System of Japan*

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as well as the Yokohama Specie Bank, for foreign exchange. For mortgaging immovable property, and especially for the benefit of agricultural interests, the Industrial Bank of Japan and the Banks for Agriculture and Industry were established. For the issue of shares and debentures and for trust business, and especially for introducing foreign capital into this country, there is the Hypothec Bank. Besides those banks, there are the Bank of Formosa and the Hokkaido Bank, which act as financial organs for the colonies. Financial negotiations between Japan and Korea will be transacted by the newly established Central Bank of Korea. Another system, developed to a very high degree of perfection, is that of Postal Savings, distributed throughout the country, for transacting small exchanges, and also for receiving small deposits.

The banking system of Japan may be considered perfect at present and adequate to meet the prevailing condition of the country, and the efficiency of the Bank of Japan as the center of the banks of the whole country is very marked. As a matter of fact, however, in spite of the power and authority absolutely vested in the Government to inspect the banks' business, the method of exercising that authority is still imperfect and leaves much to be desired in the way of its enforcement.

There is also another point which calls for improvement, namely, the imperfect and undeveloped condition of the stock exchange of this country. The present system is liable to abuse, and consequently a considerable degree of inconvenience is felt in mercantile transactions involving

negotiable instruments, which are so closely related to financial business in general.

AMENDMENTS PROPOSED BY BARON SAKATANI.

Regarding the present system of the Bank of Japan as the Central Bank, I propose the following three amendments:

- (1) The augmentation of its capital. The present capital of the Bank is 30,000,000 yen. This capital was decided on fourteen years ago. Japan's commerce and industry have since developed very rapidly, and the financial expansion has been correspondingly great. Government bonds and treasury funds have increased several times over. Moreover, by the alteration of the currency system the original 1 yen now corresponds to 2 yen, which necessitates at least the doubling of the amount of the capital of the Bank.
- (2) The extension of the limit placed on the note-issuing capacity of the Bank against the security reserve. According to the present law, the amount of notes to be issued by the Bank of Japan without specie reserve, but against commercial bills and national bonds (which are classed as security reserve), is limited to 120,000,000 yen. This regulation is ten years old, and the present condition calls for an extension on the same grounds as stated in the preceding paragraph. It would be proper to increase the sum to 150,000,000 yen.
- (3) Alteration of the amount of the tax to be paid by the Bank for the notes issued.

According to the present law, the Bank has to pay a tax corresponding to 12/1,000 per annum of the average amount of the notes issued every month against the secur-

## *The Banking System of Japan*

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ity reserve; and on notes beyond the maximum amount, issued under sanction of the Government, the Bank has to pay a tax at the rate of not less than 5 per cent per annum. Of the above two kinds of taxes the one which is levied on account of the issue of notes beyond the maximum amount requires no alteration, for this provision induces the Bank to withdraw the issue as soon as possible; but with respect to the other, the tax obligation is apt to impair more or less the efficiency of the Bank's operations. It would be better to rescind this regulation and replace it with an arrangement whereby the Bank, on realizing an excess of profit over a certain fixed rate, should be made to pay a certain amount to the Government. Such a method would be quite a proper one in taxing a privileged juridical person like the Bank of Japan.

### CERTAIN COMPARISONS MADE.

The system followed in the Bank of Japan having been modeled after the system in vogue on the European continent, as already stated, there is no very great difference from the European system in its operation as regards the issue of convertible notes, the maintenance of specie reserve, the method of absorbing bullion, and the adjustment of the rate of interest. There are, however, minor differences, according to the peculiar conditions prevalent in each of the countries where a similar system is followed.

The Yokohama Specie Bank is an institution peculiar to Japan. When the country, after a long seclusion, was suddenly opened to foreign intercourse fifty years ago, there existed no financial organ for the newly created foreign trade, and it was for the purpose of affording the

necessary medium that the Bank was established. Consequently there is no bank in any other country that can be compared with it.

Finally, I venture to say that without a Central Bank I do not see any way whereby national finances and the economic system can be consistently developed. I have studied American finance for some years, and have come to the conclusion that the solution of the problem may best be sought in the unification of the system by the issue of convertible notes and the establishment of a Central Bank.

# THE BANKING SYSTEM OF JAPAN.

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## III.

### OPINIONS OF S. NARUSE,

*Financier.*

Any discussion of our present banking system must begin with the origin and history of the banking business in this country, and involve a statement of the original laws forming the bases for the present system.

There were in operation in feudal days some organs resembling banks, under the names of *Kwase-Gumi* (Exchange Company), *Kwase Goyotashi* (Exchange Contractors), *Kake-ya* (Credit House), etc., conducting business connected with the receipts and disbursements of the Feudal Government, or acting as financial agents for feudal lords, as well as giving pecuniary assistance to business men. But the history of real banking in Japan begins with the promulgation of the National Bank Regulations in November, the 5th year of Meiji (1872).

The National Bank Regulations were based mainly upon the National Bank Act of the United States of America. The regulations, in their original form, provided that the national banks should deposit with the Government paper equal to 60 per cent of their capital, for which amount the Government gave the *Kinsatsu* (paper money, or, literally, gold notes) exchange bonds, on the security of which bank notes to the same amount were to be issued. On the other hand, a specie reserve equal in amount to 40 per cent of their capital was to be provided for the conversion of these bank notes. By this

means the Government aimed at a speedy withdrawal of inconvertible notes and at meeting the needs of the financial world. In those days there was no difference in value between paper and specie, and the system worked well and smoothly.

The conditions, however, became changed when, with the 7th year of Meiji (1874), the evil effects of the over-issue of government paper money began to be felt, and as a natural result of the increase of the imports of the country there began to take place a greatly increased export of specie. In consequence of this the price of gold coin rose daily, and the depreciation of paper money rapidly set in.

Government paper money, in June of the 8th year of Meiji (1875), showed an exchange rate of 1,017-1,018 yen for 1,000 gold yen. The demand for the conversion of notes, made upon the specie reserve of the national banks, became very large. The notes issued were immediately returned for conversion, having no time for circulation, and the banks sustained considerable losses because of the necessity for keeping a supply of specie on hand for the purposes of exchange. The notes intended for circulation lay useless in their vaults, and one of the four banks then existing had not been able to issue a note since opening for business. Such being the case, the specie reserves in the banks almost disappeared and paper money was gradually decreasing in circulation and losing its usefulness. The business of the banks became difficult, and no one dared to apply for the establishment of a national bank. What the Government at first hoped for was not realized, and it was apparent to everybody that the system

## *The Banking System of Japan*

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of bank notes, convertible with specie, could not permanently be maintained.

At this time the Government determined to apply the Hereditary Pension Bonds—by way of reforming the *Han* (Clan) system as a result of the restoration—to the *Kwazoku* (Nobles) and the *Shizoku* (Gentry or Samurai) for their hereditary pensions or their pensions for merit. This necessitated an issue of government loan bonds amounting to 174,000,000 yen, and in order to create a demand for these bonds, and also to stimulate the establishment of national banks, the national-bank regulations were revised in August, the 9th year of Meiji (1876), chiefly to the effect that bank notes should be issued by the banks to the amount of, and on the security of, government loan bonds of over 4 per cent interest, deposited to an amount equal to 80 per cent of their capital, and that a currency reserve for conversion should be provided to the extent of 20 per cent of the capital, or a quarter of the actual amount of issue. But this currency reserve meant in reality government paper money, to which the bank notes became convertible. By this reform the convertibility of the bank notes with gold was changed to their convertibility with currency. The bank notes thus becoming inconvertible notes, and conditions being thus changed, the establishment of national banks was greatly encouraged, and in a few years their number increased to 150. When this number tended to increase still further, the Government, seeing that if more establishments were granted the inevitable result would be the expansion of inconvertible notes, and that the evils involved would be disastrous, issued special regulations, with a view to

restricting the number of national banks, and when they numbered in all 153 no more were established.

On the other hand, there remained in circulation government paper money to the amount of over 100,000,000 yen, besides the national-bank notes of inconvertible character issued recently owing to the revision of the national-bank regulations. The difference between paper and specie became greater and greater. Prices rose and bonds depreciated in consequence of the depreciation of paper, so that both the Government and the people began to regard with suspicion the circulation of the inconvertible notes, as well as the bank notes. The adjustment of paper currency had become an object of prime importance, and it was generally felt that the unification of the currency system necessitated the establishment of a Central Bank, which should alone be privileged to issue convertible bank notes. The outcome was the Bank of Japan.

Central Banks in other countries differ one from another in their organization, but they are all alike in that they serve as supreme organs for the regulation of the monetary circulation of the countries in which they are established. In introducing into this country the central-bank system the Government studied the systems in Europe and America, and finally decided to adopt that of the Central Bank of Belgium. It is needless to say that at the same time the Government, while framing the new central-bank system after the system prevailing in western lands, fully considered the particular conditions prevailing in Japan. Thus in June, the 15th year of Meiji (1882), the regulations concerning the Bank of

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Japan were issued, and its foundation followed immediately. In May, the 17th year of Meiji (1884), the convertible bank-note regulations were also issued.

The circulation of the Bank of Japan convertible notes gradually increased, and the withdrawal of the government paper money and the national-bank notes was simultaneously carried out. Although in July, the 21st year of Meiji (1888), some amendments were introduced into the convertible bank-note regulations, and there were several other subsequent reforms, yet this date marks the foundation of the present currency system of Japan.

The following is the gist of the present Bank of Japan convertible-note regulations:

The Bank of Japan shall keep gold or silver coins, or bullion of those metals, as a conversion reserve, equal in amount to the convertible bank notes issued. The amount of silver coin and silver bullion shall not exceed one-quarter of the whole amount of conversion reserve.

The Bank of Japan may, outside the provisions of the preceding paragraph, further issue convertible bank notes, on the security of government bonds or treasury bills, or other bonds and commercial bills of a reliable nature, within the limit of 120,000,000 yen; of this amount, however, 27,000,000 yen shall be set apart to be issued after the first day of January, the 22d year of Meiji (1889), in installments, from time to time, in proportion to the amount of the national-bank notes redeemed.

The Bank of Japan may, outside the provisions of the two preceding paragraphs, make a still further increase of convertible bank notes, in order to meet special emergencies of the market, and, with the special permission of

the Minister of Finance, on the security of government bonds or treasury bills, or other bonds or commercial bills of a reliable nature. The notes shall be subject to a special tax of not less than 5 per cent per annum, the rate of interest to be fixed in each case by the Minister of Finance.

The Bank of Japan shall supply by way of loan not more than 22,000,000 yen to the Government, without interest, for the purpose of redeeming the government paper money. The period of time within which this loan shall be repaid by the Government and the rate of annual installment shall be fixed by the Minister of Finance.

Now that the business organization of the Bank of Japan was complete, the regulations were revised so that the national banks' term of business should expire at the end of twenty years, and that if they desired to continue their business thereafter they might do so only by becoming private banks. At the same time the rules for redeeming the national-bank notes were laid down and put into operation. At the expiration of their term of business most of the national banks were reorganized and have continued their business till this day purely as private commercial banks, acting as organs of general trade, in accordance with the bank regulations promulgated in August, the 23d year of Meiji (1890).

The revision of the national-bank regulations in the ninth year of Meiji (1876), side by side with the issue of the hereditary pension bonds, gave an impetus to the establishment of banks, and in about the twelfth year of Meiji (1879) the financial organs of the country for domestic purposes were nearly complete; but for foreign

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trade purposes there existed only two or three branches or agencies of foreign banks. At this time the paper money increased in circulation, the difference in value between paper and silver became considerable, resulting in the outflow of specie abroad, which brought about a scarcity of gold and silver coins and consequent distress in commercial and financial circles.

In order, therefore, to lay the foundations of the financial welfare of the country, the establishment of an organ for facilitating the operations of the money market became of paramount importance, and in November, the twelfth year of Meiji (1879), the Yokohama Specie Bank was established. This bank was created after the promulgation of the national-bank regulations, and was for the time being subject to their control. But, with the gradual expansion of its business, and in order to distinguish it in connection with foreign commercial intercourse from the ordinary banks, the Government issued the Yokohama Specie Bank Regulations in the twentieth year of Meiji (1887), and gave the Bank a special position of its own. The new regulations have since placed the Bank under government control, and its chief object is to act as a financial organ for foreign trade. It is now one of the most important cogs in the financial machinery of the country.

Seeing that the Central Bank was already founded, with numerous ordinary banks under it scattered all over the country, and that a foreign trade organ, the Yokohama Specie Bank, was also established, it looked as if the mechanism for commercial purposes was nearly

complete. These provisions, however, from the viewpoint of scarcity of capital, were found to be still insufficient, as no such organs existed for the benefit of agriculture and industry. To correct this defect, the Government established the Hypothec Bank of Japan and the Agricultural and Industrial Banks as monetary organs for agriculture, and the Industrial Bank of Japan as a parallel institution for industry.

The Hypothec Bank of Japan acts mainly as the financial medium of agriculture, and was founded on the lines of the Crédit Foncier de France. Its principal business consists in making long-period loans at low rates of interest on the security of real estate, for the purpose of the improvement and development of agriculture and industry. It has as its local organs the Agricultural and Industrial Banks established for the same purpose, and they co-operate to provide financial facilities for agriculture and industry, and by this means to enhance the national wealth. To obtain the funds for loans, these banks are authorized to issue debentures, their business being conducted under strict governmental supervision.

The organization of the Industrial Bank of Japan is based largely on that of the Crédit Mobilier of France, being designed as a financial organ for industry just as the Hypothec Bank is for agriculture. Its scope is limited, in the main, to making loans on the security of national loan bonds, local loan bonds, or shares of companies, receiving deposits of money, and taking charge of goods intrusted to it for safe-keeping. It undertakes a trust business in relation to local loan bonds or the debentures and shares of companies, and makes loans to public

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bodies organized by law. The Bank is thus precluded, to a certain extent, from carrying on business similar to that of ordinary banks, but it is endowed with the privilege of issuing debentures to an amount of ten times its capital. The business management of this bank is also under the direct control of the Government.

Besides the above-named banks there are the Colonial Bank of Hokkaido and the Bank of Taiwan (Formosa), but as these are special organs, essentially colonial in their nature, and have little relation to the general economic situation, they will not be dealt with here.

To explain the relation of the Government to the Bank of Japan, it must be premised that it differs from ordinary banks in having the privilege of issuing currency notes, and it is through this privilege that the Bank has various dealings with the Government. As already stated, the Bank of Japan was originally created for the purpose of withdrawing government paper money and national-bank notes, changing and unifying these into paper notes having specie reserve. The Bank is therefore legally bound to make loans without interest to the Government to a limit of 22,000,000 yen for the purpose of redeeming the government paper money. It manages free of charge the receipts and expenditures of the National Treasury and transacts all business concerning the national loans. Formerly the receiving of moneys of the National Treasury and their disbursement were intrusted to the so-called exchange dealers. These exchange dealers, however, were a group of private individuals, private banks, and national banks, and their ability and credit were considered

doubtful. As the volume of cash receipts and disbursements increased the domination of these exchange dealers became objectionable, and in the Bank of Japan act it was specified, in article 13, that the Government might intrust to the Bank of Japan the function of receiving and disbursing state funds. According to the government treasury regulations there are the central, the main, and the branch treasuries. The Central Treasury is located in Tokyo, a main treasury in each of the municipalities and prefectures and in Sapporo, Hakodate, and Nemuro, and the branch treasuries in various places where the Minister of Finance deems their location necessary. The branch treasuries are supervised by the main treasuries; the Minister of Finance exercises superintendence over all the treasuries, and, as occasion may require, he dispatches officials to any treasury office for the inspection of treasury books. Now this treasury business is managed by the Bank of Japan, and the Bank is solely responsible for the custody, receipts, and disbursements of cash. The affairs of the main and branch treasuries in various places are dealt with at the local branches or agencies of the Bank of Japan. The governor of the Bank is the cashier of the government treasury, and the heads of the Bank's branches or agencies are his proxies.

On the convertible notes issued by the Bank of Japan on security reserve the Government imposed a tax at the annual rate of 1.25 per cent for the total issue, less the amounts lent to the Government or others without interest or at any annual rate of interest not exceeding 1 per cent. As regards the issues in excess of the limits specified by law, a tax is levied at a rate of not less than 5 per cent

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per annum, fixed by the Minister of Finance at the time of such issue.

Among the relations of the Government with the Bank of Japan, those specified by the Bank's act are as follows:

- (1) Any person desiring to become a shareholder of the Bank of Japan shall obtain the permission of the Minister of Finance. (Art. 6 of the act.)
- (2) For the purpose of buying or selling government bonds the Bank shall obtain the permission of the Minister of Finance. (Art. 16 of the act.)
- (3) The governor and vice-governor of the Bank of Japan shall be appointed by the Government. The directors of the Bank shall be selected by the shareholders of the Bank at their general meeting and shall be approved and appointed by the Minister of Finance. (Arts. 18 and 19 of the act.)
- (4) In making advances in current accounts or loans for a fixed period the Bank of Japan shall obtain the sanction of the Minister of Finance as to the amount of such advances and loans and the rates of interest to be charged. (Item C of Art. II of the act.)
- (5) The Government superintends all the business of the Bank of Japan and restricts or forbids the acts of the Bank not conforming to the Bank's act or articles of association or contrary to the interests of the Government. (Art. 24 of the act.)

The Yokohama Specie Bank is not directly endowed with any privilege by the Government, but is entitled to a loan of 20,000,000 yen at the low interest of 2 per cent from the Bank of Japan as a fund for foreign exchange. Although this constitutes a connection between the Specie Bank and the Bank of Japan, it should be noted that this is a special arrangement made by the Government. The

Bank is charged, on the other hand, with the duty of handling, by the Government's order, matters concerning the government loans and moneys in connection with foreign countries. Thus the Yokohama Specie Bank's connection with the Government is less than that of the Bank of Japan, but it is under the control of the Minister of Finance, who has the right of supervision and approval in all the business matters of the Bank, as well as in the appointment of its directors.

Let us now glance at the relations between the Bank of Japan and the ordinary banks. It goes without saying that the business of ordinary banks consists principally in handling their own capital and the deposits of the public, but in case of further need of capital they approach the Bank of Japan for the discounting of commercial bills or loans on security. The Bank of Japan, since its establishment, has made a practice of aiding the ordinary banks, and there exists a considerable gulf between its rate of interest and that of ordinary banks—that is, the discount rate of the Bank of Japan is, as a rule, much lower than that of the ordinary banks. The unavoidable result of this was that some banks, taking advantage of the situation, made it their chief business to earn the amount of the difference for themselves by becoming intermediaries between private individuals and the Bank of Japan. We must here observe that the relations between our Central Bank and our ordinary banks differ greatly from those in foreign countries, especially from those in England, Germany, and France. This difference lies in the special circumstances under which the Bank of Japan was first established, which, indeed, have influenced the general

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banking system of this country not a little. The business methods of the Bank of Japan always tend to affect those of the ordinary banks. For instance, if, in consequence of the Government's financial condition, the capital of the Bank of Japan becomes tight, the money market will soon be affected thereby. Thanks, however, to the steady evolution of this country's economic conditions, the practice adopted at the earlier stages by ordinary banks of making profit by the difference of interest is gradually disappearing.

In considering the advantages and disadvantages of the banking system in this country, we shall consider the two following questions:

- (1) Whether there should be special banks respectively for agriculture, industry, and commerce, or whether one bank should act for all three lines.
- (2) Whether the banks should be separately and independently established, or whether the branch system should be adopted.

In England and America one bank performs the financial functions for agriculture, industry, and commerce, but on the Continent of Europe there are special monetary organs for each of the three branches. To arrive at a conclusion as to which of the two systems is the better, we shall discuss the different ways in which the capital is utilized in the three cases. The following are the three points in which the nature of the capital varies in the three lines:

- (1) As regards the period of redemption, capital has the quickest return in commerce. The money invested is brought back immediately by the disposal of

the merchandise, and is again used for other goods, with the result that the term of credit is not necessarily long. In industry the capital becomes fixed in machinery, factories, etc., but the money invested in raw materials is restored as soon as the materials are manufactured and sold. On the other hand, the capital for agricultural purposes is all spent on land, implements, etc., and becomes fixed, except a small portion spent on fertilizers, seeds, labor, etc. The return of capital is slowest in agriculture, being effected gradually and by annual installments.

- (2) Regarding the certainty of redemption, the capital invested in commerce is influenced only by artificial market fluctuations, which govern the business profits, while agricultural pursuits are affected by natural causes, uncontrollable by human energies, so that, to this extent, the return of capital in agriculture is uncertain.
- (3) As regards the renewal of capital, agricultural pursuits, unlike the other two lines, require little, the period for which the capital becomes fixed being long, unless the land purchased meets with some catastrophe. In industry, renewal is necessary to a certain extent owing to the wearing out of plants and buildings and to the sale of the articles of manufacture. In commerce the term of fixed capital is shortest, renewal being necessitated on the sale of goods.

As the operations of capital vary thus in the three pursuits, there should accordingly be various kinds of banks for supplying the capital.

In Japan we have as mercantile banks the ordinary banks, with the Bank of Japan as their center; as industrial

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bank, the Industrial Bank of Japan; as agricultural bank, the Hypothec Bank of Japan. We believe that, in this respect, our system of monetary organs is perfect.

With regard to the single and branch systems of banks, practice differs in different countries according to the circumstances under which the banks have developed. In some countries there are numerous independent banks, and in others a few large banks have branches under them. For instance, the United States of America belong to the former and Scotland to the latter. There are advantages and disadvantages in both systems, but to the unbiased mind it would seem that the disadvantages of the branch system are outweighed by its advantages. Among the latter may be mentioned:

- (1) The increased efficiency of capital: the kinds of capital may be augmented and also may be easily altered. Sudden change in the rate of interest may consequently be avoided and elasticity in business management may be secured.
- (2) The extension of the advantages of the banking system to remote parts of the country.
- (3) Elimination of rash competition among banks.
- (4) Reliable and timely reports on economic conditions from various districts.
- (5) Economy in business expenses.

The above are the advantageous points of the branch system, and the following may be stated as its disadvantages:

- (1) The difficulty of controlling the branches.
- (2) The possibility that the failure of one branch may affect the main bank as well as the other branches.

The advantages of the branch system as above pointed out are, in the main, inherently beneficial to the public interests, while the disadvantages are rather evils that may be avoided if proper care is exercised.

In the banking system of Japan, independent banks of small means are widespread, owing to circumstances special to the country, many of them being bequeathed by the old national-bank system. Men of experience early urged the necessity of amalgamating banks, and a special law known as the Law for the Amalgamation of Banks has been enacted. The number of branch banks has recently increased, but we are not yet at the stage of the perfect branch system.

We have so far reviewed the general features of our banking system; we shall now proceed to treat of our central bank system.

Our Central Bank, the Bank of Japan, is the only organ in the country for issuing paper notes, and is based on the so-called centralization system of issue.

A note-issuing bank system may be established on one of two principles—centralization or separation. To decide on their relative merits, we will here enumerate the different points in the former that are positively beneficial to the interests of the financial as well as the political world.

Viewed from the financial standpoint, the centralization system is superior in the following respects:

- (1) A country has at times to make large payments in specie to foreign countries in connection with trade or loans raised. In such cases, if the separation system is adopted, the specie reserves in different banks are collected, thereby affecting the money

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market in the same way as an outflow of specie would affect it. If the Central Bank system is adopted, and the specie reserve remains concentrated from time to time to provide for such emergencies, the bad effects will be minimized.

- (2) In the centralization system, the Central Bank has the power of influencing the other banks, and can readily accumulate the specie reserve by means of discounts, the elasticity of currencies being thus amply secured.
- (3) As the Central Bank handles immense capital, it has real power to supply capital, and its responsibility for the money market is unique, since it clearly stands as a public organ. If a panic sets in, the Central Bank will be able to restore order much more easily and more effectively than in the case where banks with little credit abound.

Viewed from political and economic standpoints, the centralization system is also superior in the following respects:

- (4) If the Central Bank carries on its business as the central organ in the market and continues to receive the public credit, the Government will be enabled in time of serious emergencies to meet its own requirements by borrowing the funds the Central Bank collects on its own credit.
- (5) As a country's finances expand, the receipts and disbursements of the National Treasury will surely have a most important effect on the monetary interests of the country, and if the Government makes the National Treasury the custodian of taxes collected and all the other revenue, and continues to do so without moving them till their due dates of disbursement, it will, as a matter of course, greatly hinder the circulation of capital. In the

separation system of banks, the above contingency may become unavoidable, but under the centralization system there is the reliable Central Bank, to which the Government intrusts the national treasury receipts and disbursements, and the Bank may utilize the receipts in the market till their due dates of disbursement, the bad effects on the markets of the accumulation of receipts in the National Treasury being thereby minimized.

The above are the general advantages attending the centralization system, which have led our Government to endow the Bank of Japan with the exclusive privilege of issuing paper money, at the same time maintaining a strict supervision of the Bank's business management and the appointment of the governor, directors, etc.

As is the case with ordinary banks, the Central Bank attaches special importance to loans and discounts, and these form its chief source of profit. Government interference may inconvenience the Bank, but is, nevertheless, necessary, as the bills, bonds, etc., received by the Bank in making loans and discounts, constitute a part of the reserve fund for convertible notes. As the credit of convertible notes is secured and established by the regulations for issuing bank notes, the Government must control the selection of bills, bonds, etc., to be received, directing the business of the Bank and controlling the nomination of its staff.

We shall now further touch upon our methods of issuing convertible bank notes. In the convertible-note regulations of our Central Bank the principle followed is to provide the full amount of specie reserve. A fixed amount of issue is also allowed against securities, an excess issue

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being permitted, in case of necessity, on the payment of a tax at a rate of not less than 5 per cent per annum. This is what is called the elastic-limitation mode of issuing, and much resembles the German method, on which it was originally modeled. But the point in which our mode excels all others is that the percentage of the tax imposed for excess issue is on each occasion fixed by the Minister of Finance according to the circumstances then obtaining. The object of taxing excess issue is to check over-issue in meeting the urgent requirements of the time when the money market becomes tight and the rate of interest tends to rise. Under the régime of a fixed rate, if the rate is too low, the excess issue will be made at even ordinary times; if the rate is too high, the excess issue will be made only after the abnormal rise of interest, and the proper time of making excess issue will be missed. The rate of the tax should not therefore be a fixed one, but should be, as in our own case, buoyant and flexible according to the needs of the time.

In the German system commercial bills only are available for the reserve, but in our system government bonds, treasury bonds, or other bonds of reliable nature are used for the purpose, besides commercial bills. Experience having shown the uncertainty of refunding public loans in critical moments, the exclusive use of commercial bills may be ultimately desirable; but here in this country, where commercial transactions are not yet fully developed and the supply of bills is insufficient, the use of public bonds as reserves can not for the time being be entirely abandoned.

Considering all points here explained, our banking system may be said to be nearly perfect in the main, though in its details there is room for improvement. However, we are still backward in our banking achievements as compared with Europe and America. This is to be attributed to the fact that our banking system is only a little over thirty years old, and its development is not complete, and that our commerce and industry in general, though they have made gigantic strides, can not yet vie with those of western lands.

We shall now recapitulate the system, administration, and business of our Central Bank, comparing them with those of the Central Banks in foreign countries, especially in England, France, and Germany.

The Bank of Japan may issue notes on the security of government bonds, treasury bills, commercial bills, etc., to a limited amount, besides issuing convertible notes with specie reserve; further, if the market needs more currency for circulation, the Bank is also enabled to issue notes with security, provided the Government permits it, and a tax of 5 per cent or over per annum is paid. In the case of the Bank of England the issue with specie reserve and the limited issue with security reserve are alone permissible, and the excess issue of our system is not allowed. It is customary in the Bank of England for its issuing department always to maintain the security reserve at its full amount, and the notes are issued to their full amount, which always remains without any increase or decrease, the elasticity of notes being insured by virtue of the deposit reserve in its business department. If a large amount of specie is required owing to a special market con-

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dition, the increase is invited by means of a movement in the interest rates.

The system of our Central Bank is very much like that of the Imperial Bank of Germany. While in our system the providing of full amount specie reserve is the principle, the proportional reserve system of providing specie to the minimum amount of one-third of the amount of convertible notes issued is to a certain extent adopted by the German bank; and whereas the minimum rate of tax on excess issue is 5 per cent in ours, the rate being fixed by our Minister of Finance on each occasion, the same is fixed at 5 per cent per annum all around in the German bank.

The Bank of France differs totally in principle from the central banks of Japan, Germany, and England. In France the maximum emission system of notes is followed, and the maximum amount of notes to be emitted is fixed. The kinds and amounts of conversion reserve are left entirely to the discretion of the note-emitting bank, there being no legal restrictions thereon.

As to the administration of Central Banks, they are in all countries under the strict and careful supervision of the respective Governments. In the manner of electing and appointing the principal officials, the Bank of Japan closely resembles the Bank of France. In both cases the nomination of the governor and vice-governor is made by the Government, the directors and officials under them being elected by the shareholders, and the discount committee for examining the bills to be discounted is elected from among the stockholders. The points of detail in which they differ are that where there are one governor

and two vice-governors in the Bank of France, the former being elected from among the stockholders holding 100 shares or over, and the latter from among those holding 50 shares or over, there are in our Bank one governor and one vice-governor, nominated by the Government, and only the directors and the officials under them are chosen from among the shareholders and appointed by the Government. In our system there is also a special provision whereby the members of the discount committee discharge the duties of comptrollers. In the Imperial Bank of Germany the organization is like that of a government office, the regulations being very rigorously drawn up. Its supervision is vested in a board of inspection, with the Imperial Chancellor as chairman, and four councillors, one of whom is appointed by Imperial nomination, the other three being nominated by the Bundesrat, or Federal Council. The administrative board, under the control of the Imperial Chancellor, manages the business of the Bank, which, in its dealings with the public, is represented by this board, consisting of a president and a few directors, whose decisions, made by a majority and approved by the Imperial Chancellor, are final. The president and directors of the administrative board are chosen by the Bundesrat and appointed by Imperial nomination. In the Imperial Bank of Germany the shareholders merely elect a committee consisting of fifteen of their number, who express the opinions of the shareholders regarding the Bank's business for submission to the administration. In the Bank of England the court of directors consists of the governor, deputy governor, and twenty-four directors, the latter being elected from among the stockholders, but the

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governor and deputy governor from among the directors. According to the custom of the Bank of England, the governor consults with the cashiers regarding the management of the affairs of the bank. The cashiers are appointed and organized by one who was formerly the governor or deputy governor, or who is in position to succeed to either of the two positions.

As regards the details of management in the Central Banks in Japan and abroad, we can not here make particular comparisons; still in all countries the Central Bank serves as the supreme organ in the money market and the center of financial operations, also as a medium for developing the country's commerce and industry. Thus the principal object of a Central Bank is the same everywhere. The kinds of business transacted by the Central Banks in different countries are as follows:

### THE BANK OF JAPAN.

Discounting or purchasing bills; buying and selling gold and silver bullion; receiving deposits of all kinds; accepting the custody of coins and documents; making advances in current account or loans for a fixed period on the security of government bonds, treasury bills, or other bonds guaranteed by the Government. The bills discounted by the Bank of Japan shall be such as are indorsed by two or more persons and payable within one hundred days; provided that goods or warehouse certificates for the goods have been surrendered as security, the bank may discount bills carrying only one indorsement.

# *National Monetary Commission*

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## THE BANK OF ENGLAND.

Buying and selling specie, bullion, and bills of exchange; discounting bills; receiving deposits; making loans on securities.

## THE BANK OF FRANCE.

Discounting bills payable within three months; receiving deposits; accepting the custody of coins, precious metals, and documents; making loans on the security of government bonds and company debentures; issuing short-term bills.

## THE IMPERIAL BANK OF GERMANY.

Buying and selling gold and silver bullion and coins; discount, purchase, and sale of bills payable within three months and carrying two or more reliable indorsements, and of the debentures issued by juridical persons in the realm or states of Germany and redeemable for face value within three months; making loans with interest for not more than three months and on the security of movables; receiving deposits.

Besides the above, the receipts and disbursements of the national treasury funds and the handling of principal and interest of the national loans are intrusted to the Central Bank in every country. The kinds of business transacted by the Bank of Japan are as already mentioned, but twenty years ago, when the money market was in straitened circumstances, the discounting of bills with security of company shares was undertaken in order to facilitate the supply of capital for the company shares; and as the shares of companies of reliable standing are

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now accepted as securities for bills discounted, the restriction on company shares as securities has been practically done away with.

With reference to the discount tariff, the central banks in England, France, and Germany generally put the official rate at a higher point than the rate of ordinary banks, and if the market becomes tight and the rate of ordinary banks rises above that of the Central Bank owing to the scarcity of funds in the market, then the Central Banks, in these countries, come to the rescue of ordinary banks; but on the contrary, the Bank of Japan keeps the rate at a low point at all times, and makes it her constant object to prop up the ordinary banks. In regulating the influx and outflow of specie consequent upon international relations, the Bank of Japan, the Bank of England, and the Imperial Bank of Germany all act alike in varying the discount rate—a device which has proved effectual. The Bank of France alone follows a different course and strives to keep a fixed rate. To control the outflow of specie, however, the Bank of France charges a certain rate of commission on the conversion of notes to gold. Although this conversion premium seldom exceeds seven or eight thousandths of the amount of conversion, it has successfully controlled the specie outflow and protected the specie reserve of the Bank. The measure seems to be one that is necessitated in France by the coinage system of that country.

The Yokohama Specie Bank is a special bank carrying on business under regulations differing from those for ordinary banks. Its business is, however, similar to that of an ordinary bank, except that its main object is to aid

foreign trade. The only reason of its being under government control, with special regulations, is that the Bank is privileged to borrow funds from the Bank of Japan at a low rate of interest for the purpose of facilitating foreign trade, and also that it deals with the government moneys abroad. The Yokohama Specie Bank is not the only bank in Japan engaged in foreign transactions, nor is it confined to such transactions; it does business as an ordinary bank as well. We can not here compare in detail this bank with the large financial organs in foreign countries, but must be content to give the essential points of the regulations and the articles of association of the Yokohama Specie Bank, as follows:

“The Yokohama Specie Bank shall be a limited association. The capital of the Bank shall be 24,000,000 yen. The shareholders of the Bank shall be Japanese subjects only.

“The number of directors shall not be less than five, the number of inspectors shall not be more than three, and they shall be elected at an ordinary general meeting of shareholders from among the shareholders. The election of the directors shall be sanctioned by the Minister of Finance.

“The president and vice-president shall be chosen by the directors from among themselves. Their election shall be sanctioned by the Minister of Finance.”

The business of the Bank is: The purchase and sale of foreign bills of exchange, credits and documentary; the purchase and sale of inland bills of exchange, credits and documentary; loans; deposits of all kinds, and custodies; discounting and collecting bills of exchange, promissory notes, and other negotiable paper; exchange of coins or

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moneys; purchase and sale of public bonds, gold and silver bullion, and foreign coin. The Bank shall, when so ordered by the Government, act in all matters connected with public loans or government moneys in foreign countries.



# THE BANKING SYSTEM OF JAPAN.

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## IV.

BY

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### INTRODUCTION.

It is not my purpose in these pages to present a comprehensive survey of the history and methods of banking in Japan. To do so would involve needless repetition of matters which have been set forth by distinguished Japanese contributors to the publications of the National Monetary Commission, whose knowledge and understanding of the subject must be far greater than a foreign observer could possibly possess. I shall concentrate attention upon a very few aspects of Japanese banking, selecting those which seem most likely to be of value or interest to American readers and those the significance of which can best be understood when considered in comparison with banking methods and practice in the United States or in Europe. I shall try to explain why, after a short trial of a banking system modeled upon that of this country, it was transformed into one with a central bank as its guiding force. I shall then consider the relations between the Bank of Japan and the other banks of the country. This is a matter of the first importance because, owing to the rather slight development of branch banking, Japan affords a unique instance of a central bank

working among a numerous company of other banks. A central bank established in this country would find itself in a similar situation. It therefore seems desirable to make the relations between the Bank of Japan and the other banks the central problem for analysis in studying the operation of the Japanese money market.

#### NATIONAL BANKS IN JAPAN.

The reopening of Japan to intercourse with the Western world dates from the commercial treaty with the United States negotiated by Commodore Perry in 1854. During the following fifteen years little apparent advance was made toward the adoption of any part of the alien civilization aside from its methods of making war. Opposition to the foreigner was still well-nigh universal among the people, and the country was almost constantly in turmoil, which culminated in 1868 in the overthrow of the Tokugawa Shogunate and the restoration of power to the Imperial line of rulers. Then came a sudden change. In Japan power has always been exercised by a comparatively small class. After the restoration the handful of individuals conducting affairs recognized that the organization of both state and society in Japan needed to be transformed from a feudal to a modern basis. Since that time the Japanese have industriously adapted to their needs (not merely copied) those customs, methods, and institutions of the West which have seemed to them of practical utility. No one country has at any time been exclusively drawn upon, though at successive intervals there seems to have been a perceptible predilection for

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the ways and devices of particular nationalities. In the seventies the United States was taken as a model for many things, and among others for the law under which the first modern banking system was established in Japan.

It can not be said that this step was taken as a result of a thoroughgoing analysis of the working of our banking system in comparison with those of other countries. Indeed, many of its fundamental characteristics had not become apparent at that time. It had been in operation less than ten years and had not been subjected to a period of severe financial strain. In the autumn of 1870 Assistant Secretary of Finance Ito (later Prince Ito) was sent to the United States to study our banking and financial arrangements. After a brief examination he reported in favor of the establishment in Japan of a banking system modeled upon that of this country. Although the English system was not without its adherents, the Government adopted Ito's suggestion, being apparently much influenced by the means which it seemed to provide for substituting a convertible bank note for the inconvertible paper money then in circulation.

The Imperial ordinance authorizing the establishment of national banks was promulgated in November, 1872. Since its provisions regarding the issue of notes were the determining factor in the development of the system, other provisions of the ordinance do not call for special notice. Banks were authorized to issue notes to 60 per cent of their capital, secured by government bonds. These bonds were to be issued to the banks for an equivalent amount of the government paper money, which was

then to be retired from circulation. In addition, the banks were required to hold the remaining 40 per cent of their capital in gold as a reserve. This was not to be a special reserve against notes, but in the infancy of deposit banking it meant practically that the banks would hold a reserve of  $66\frac{2}{3}$  per cent against their circulation. It is doubtful whether a sufficient number of banks would in any circumstances have been established under these onerous conditions to bring about the retirement of the government paper, which then amounted to about 68,000,000 yen. As it happened, an insuperable obstacle was soon encountered.

As the Government had issued its inconvertible paper in rather moderate quantity the depreciation of the paper was but slight and at times entirely absent. But the simplest and most direct means of securing specie was the presentation of the convertible bank notes. Accordingly, when the course of trade required specie exports the banks found that their notes would not remain in circulation. This difficulty became apparent in 1874 when only four banks had been established with an authorized issue of about 2,000,000 yen. No more banks were opened and by 1876 the circulation of the four banks which reached its maximum of 1,356,000 yen in May, 1874, had been practically all retired.

In these circumstances a demand to which the Government could hardly refuse to accede arose for some modification of the banking law which would permit the further growth of the banking business. To this demand

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the Government was the more willing to accede on account of the pressing difficulties of its own financial position. The hereditary pensions of the nobles and samurai (the military class) were about to be commuted into bonds. If these bonds should fall appreciably in price, the stability of the Government would be seriously threatened. Accordingly, the banking law was modified, its provisions regarding note issue being radically relaxed. Under the new law notes might be issued to 80 per cent of capital against the deposit of bonds already issued, not as before against bonds issued in exchange for the inconvertible government paper in circulation. The reserve against the notes was cut down from 40 per cent of capital in gold (two-thirds of notes) to 20 per cent of capital in government paper (one-fourth of note issue). Finally, in a supplementary law of the following year the total circulation was fixed at 34,000,000 yen. New banks were now organized rapidly. By 1879 there were 153 banks and all of the authorized circulation had been taken out. Further growth of the system was therefore impossible. In the meantime financial exigencies had led to a further issue of government paper. Currency became rapidly more and more redundant with the inevitable consequence of constantly increasing depreciation. The situation of affairs is clearly shown in the table following, which gives the amount of government paper, the authorized amount of bank notes, and the depreciation of the paper in terms of the silver yen at the end of each year from 1872 to 1879.

# National Monetary Commission

[Amounts expressed in millions of yen.]

Year.	Government paper.	Bank notes (authorized issue).	Rate of ex- change of paper for silver.
1872.....	68.4	.....	1.066
1873.....	88.3	1.4	1.027
1874.....	101.8	1.9	1.037
1875.....	99.1	1.4	1.009
1876.....	105.4	1.7	.981
1877.....	105.8	13.6	1.030
1878.....	139.4	20.3	1.217
1879.....	130.3	34.0	1.336

The banks were but slightly responsible for the depreciation since the Government had borrowed 15,000,000 yen in bank notes from one bank (the Fifteenth National Bank) organized by the nobles, which in capital and consequently in right of issue nearly equaled all the other banks taken together. For nearly three years following 1878 there was little pronounced change in the total volume of paper money in circulation. Government issues reached their highest point in January, 1880, at 136,000,000 yen. Thereafter, by the adoption of moderate economics the Government was able to retire about 16,000,000 yen by October, 1881, the volume of banknotes remaining stationary. Depreciation, however, had continued, the reduced demand for money on account of inactive business more than offsetting the reduction in the amount of paper money afloat. The most extreme point of depreciation was reached in April, 1881, 1.815 for the silver yen, and there was but little improvement to October of that year. At that time Mr. (later Count) Matsukata became minister of finance. At once rigid

economies were introduced and the volume of government paper was rapidly diminished from 120,000,000 yen to 93,000,000 yen at the end of 1884. This was accompanied by a slight reduction of 3,000,000 yen in the volume of bank notes. At the same time a specie reserve was accumulated by the Government in preparation for the resumption of specie payments. This reserve was only 7,000,000 yen when Count Matsukata became minister of finance. At the end of 1884 it was 34,000,000 yen and a year later 42,000,000 yen. Depreciation was of course checked; it diminished slowly during 1882 and then more rapidly until at the end of 1884 it had virtually disappeared. With the growth of population and business dealings the supply of paper had been reduced to a point that permitted its entire absorption at par.

### REASONS FOR A CENTRAL BANK.

In the meantime preparations were being made to relieve the Government entirely from direct responsibility for the circulating medium. In March, 1882, less than six months after entering upon his duties as minister of finance, Count Matsukata submitted a memorandum to the Government urging the establishment of a central bank. This memorandum, about fifteen thousand words in length, is indeed a notable state paper. The general arguments in favor of central banks were marshalled in a masterly fashion, as well as those bearing upon the special circumstances of Japan.<sup>a</sup> It is never possible from an examination of a voluminous state paper to

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<sup>a</sup> This memorandum will be found in the Report on the Adoption of a Gold System in Japan, 1899, pp. 43-67.

determine the relative importance in bringing about the adoption of a given policy to be attached to the various arguments brought forward. In this particular instance, although the report itself was concerned almost entirely with the purely banking aspects of the question, there are certain other considerations which it may be reasonably assumed had very great weight. The establishment of a central bank was certainly regarded as a means through which the Government might ultimately be relieved of all direct responsibility for the circulating medium and also from the temptation to issue paper money on future occasions of financial need. A central bank was, moreover, peculiarly in keeping with the general character of the governmental system of the country, the activities of which are to an unusual extent centralized in Tokyo.

On the purely banking side a number of reasons which seem to have been regarded as specially important may be mentioned. The system of national banks did not indeed have a fair trial. Its extension after 1879 was completely checked, at least until the Government should resume specie payments. On the other hand, leaving out of view the familiar defects of a bond secured currency, it was not a system favorable to the immediate development of an efficient banking organization throughout the country. Up to a certain point it had indeed accomplished this result and probably more quickly than would have been possible if a central bank had been established at the outset. The bonds received by the military class in commutation of its pensions were widely held throughout the country. It was therefore easy to

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establish banks until the limit of 34,000,000 yen in the total circulation was reached. Banks were established throughout the country to an extent entirely unlikely had deposit banking alone been permitted. A beginning once made, it was possible later to transfer to the central bank the monopoly of issue without causing the general disappearance of these banks. They continued as deposit banks, though many of them probably would not have been established as such institutions.

Beyond this initial stage the purely banking advantages which might be gained through a central bank were of the very greatest importance. There was an almost entire absence of arrangements between the banks for transferring idle funds to those sections of the country in which there might be a peculiarly urgent demand for accommodation. Standards of right judgment regarding the nature and function of banks were still exceedingly imperfect in most parts of the country. By means of a central bank it was possible to provide at least one institution managed in accordance with the best principles of banking practice in the Western world.<sup>a</sup>

In the second place, through a central bank it was hoped that a positive increase in the available banking capital would be secured large enough to have a pronounced effect upon lending rates. The supply of capital in Japan was increasing slowly and interest rates were exceedingly high. Even in Tokyo rates for bank loans were upon the average in the neighborhood of 12 per

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<sup>a</sup> A few of the national banks and some of the large private banks, such as those of the Mitsui and Konoike families, left nothing to be desired in this respect, but they were almost entirely found in Tokyo and Osaka.

cent, often rising as high as 18 per cent. Unlike central banks in other countries, it was expected that at all times the Bank of Japan would supply funds to the other banks, lending to them at rates somewhat below those secured by them from the business community.

Finally, it was expected that the monetary position in relation to other countries would be strengthened. In a country eager to employ all available capital in developing its resources a comparatively small amount of cash is ordinarily set aside as a foundation for its monetary and credit structure. An unfavorable balance of trade involving even moderate specie exports may seriously weaken this foundation. Particularly is this true of a country the exports of which are largely commodities which may be classed as luxuries. This is the case with Japan, the most important export of which is silk. In these circumstances, by the Japanese, and rightly, it has been deemed the wiser policy to provide means for the skillful handling of the foreign exchanges than to set aside a very considerable portion of the meager supply of capital as a foundation for the monetary and credit structure. In handling the foreign exchanges the Bank of Japan, with the closely affiliated institution the Yokohama Specie Bank, certainly promised, and has proved, to be exceedingly effective.

#### THE BANK OF JAPAN.

The Bank of Japan was founded in October, 1882, in accordance with an Imperial ordinance of July of that year. Its charter and by-laws were closely modeled upon those of the National Bank of Belgium, with the

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exception of provisions regarding the issue of notes, as to which the example of the Reichsbank was taken. At the outset the Bank possessed no right of issue, that right being deferred until the volume of paper money should be sufficiently reduced to make resumption feasible. In July, 1884, the Bank was authorized to issue notes, but on account of unexpected and unfavorable conditions in the foreign exchange market no notes were actually issued until July, 1885. A law of May, 1883, provided for the gradual retirement of the notes of the national banks. These banks were required to deposit their reserve of 25 per cent of their note issues with the Bank of Japan and to add to this amount  $2\frac{1}{2}$  per cent semiannually thereafter. The Bank of Japan thereupon became responsible for their redemption. Specie payments were resumed by the Government in January, 1886, the operation being carried through without difficulty. By June, 1888, the government paper was reduced to 49,000,000 yen and the time had apparently arrived to place the entire circulating medium in charge of the central bank. Up to this time it had issued notes under no special provisions, but, on the other hand, under the direct supervision of the Minister of Finance, Count Matsukata. As a preliminary to greater freedom of action upon the part of the management of the Bank, it seemed proper to place the right of issue upon a more definite footing. An untaxed issue of 70,000,000 yen above the specie reserve of the Bank was authorized, though 27,000,000 of this amount was only to be issued as the notes of the other banks were retired. This untaxed

issue was increased to 85,000,000 yen in 1890 and to 120,000,000 yen in 1899. The capital of the Bank was originally 10,000,000 yen. It was increased to 22,500,000 yen in 1895, to 30,000,000 yen in 1898, and in 1910 the authorized capital was further increased to 60,000,000 yen.

## DEPOSIT BANKS IN JAPAN.

The loss of the privilege of note issue proved no obstacle to the establishment of numerous banks throughout Japan. During the nineties this growth was very rapid, being, however, in considerable part due to the transformation of numerous private banks into incorporated companies. Since 1900 there has been a slow reduction in the total number of banks. There were 2,355 banks in 1901 and 2,155 in 1909.<sup>a</sup>

The decline in the number of banks has entailed no diminution in banking facilities. Branch banking is allowed in Japan and has made some progress, but much less than in most other countries. In 1900 the 2,340 banks had 1,875 branches, while in 1909 the 2,155 banks had 2,739 branches. There is still nothing in Japan like the European or Canadian banks, with hundreds of branches in places of every size. Some of the large banks in Japan have branches in various commercial centers of

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<sup>a</sup> Nearly 500 of these are savings banks, but they differ from ordinary banks only in being required to invest one-fourth of their savings deposits in bonds of the Government or of local governing bodies. Many of these banks are of very small size and there have been numerous failures among them during the last few years. I am informed, however, that the Government is about to bring forward a measure which will safeguard the interests of savings depositors more adequately. It will remove a particularly unfortunate, even though not serious, element of weakness in the Japanese banking system.

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the country. As for the rest, branch banking is a local affair. Doubtless the future will witness the same course of development that has taken place in all other countries where branch banking is permitted. There is in Japan the usual local objection to absorption, but the chief reason for the slight development of branch banking would seem to be the enormous number of things which have had to be done in a short space of time in developing a modern industrial régime. Business organization and methods, especially on the accounting side, lag behind the responsibilities which have been shouldered, and for successful operation of branches these are most essential. It is not surprising, then, that branch banking is still an almost unworked field. On account of this absence of branch banking Japan provides an example of a central bank working in this respect under conditions which would also confront the management of a central bank established in this country.

### THE BALANCE SHEET OF THE BANK OF JAPAN.

The nature of the business of the Bank of Japan may perhaps best be introduced by an examination of the table following, which contains in a somewhat abridged form the balance sheet of the bank at the close of 1903, 1905, and 1909.

# National Monetary Commission

[Amounts expressed in millions of yen.]

	1903.	1905.	1909.
LIABILITIES.			
Capital.....	30.0	30.0	30.0
Surplus and undivided profits.....	19.7	21.1	44.4
Government deposits.....	12.9	438.0	182.2
Other deposits.....	3.5	11.3	5.6
Notes issued.....	232.9	312.8	352.8
	299.0	814.2	615.0
ASSETS.			
Loans to Government.....	43.0	76.4	22.0
Loans and advances.....	34.8	62.4	31.2
Domestic bills.....	32.2	94.0	23.9
Foreign bills.....	12.2	15.2	14.8
Government securities.....	47.1	50.9	43.7
Due from other banks.....	.8	.6	.2
Deposits with agencies in Japan.....	4.8	17.8	24.4
Deposits with foreign agencies.....		373.6	228.0
Bank buildings, etc.....	2.8	3.3	5.2
Gold coin and bullion.....	120.5	119.6	221.5
Silver coin, etc.....	.8	.4	.1
	299.0	814.2	615.0

The most superficial examination of this table will show certain marked peculiarities in the operations of the Bank of Japan. Deposits are insignificant in amount except those of the Government, which have been of large, though varying, proportions since the outbreak of the war with Russia in February, 1904. Practically all of the credit operations of the Bank involve an issue of its notes. On the asset side may be first noted the enormous foreign balances, dating also from the beginning of the recent war, which have enabled the Bank to protect its gold holdings by supplying foreign exchange. These foreign balances are handled by officials of the Bank stationed abroad working through the various foreign branches of the Yokohama Specie Bank, especially those in London and New York;

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and they have been used, among other purposes, to give some stability to the market for the foreign bond issues of the Government. A considerable portion of the resources of the Bank have at all times been placed in government securities, and in addition the Government has ordinarily borrowed considerable sums from the Bank, though at present such advances have been reduced to 22,000,000 yen, a permanent loan without interest, which is a part of the price of its charter. Loans to banks and the business community, while subject to very great variations, are not normally more than 75,000,000 yen. The amount which the Bank itself contributes to the available supply of credit in the country certainly does not seem to be so much as was expected when its establishment was proposed. The management of the Bank apparently regard it primarily as an organ for regulating the currency, for handling the financial business of the Government, and as a resource in emergencies rather than an instrument for directly assisting in the development of business activities. This statement is not intended necessarily as a criticism of the management of the Bank, but rather as a criticism of some of the hopes which were raised at the time of its establishment and which were emphasized in the memorandum of Count Matsukata already referred to. After these introductory observations suggested by the examination of the balance sheet of the Bank we may now turn to a somewhat more detailed analysis of its operations, especially those which bring it into relation with the other banks.

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## THE LOANS OF THE BANK OF JAPAN.

In addition to the head office in Tokyo the Bank of Japan now has 9 branches in the most important domestic commercial centers of the country. There are no branches in important ports like Yokohama and Kobe, because foreign business is handled by the Yokohama Specie Bank. It will thus be seen that the Bank has not endeavored to cover the country with a network of branches after the manner of the Bank of France or the Bank of Germany. There has been no attempt by its means to furnish the people generally with banking facilities. Until 1897 the Bank confined its lending operations entirely to dealings with other banks, and since that time its loans to individuals do not seem to have assumed very much general importance. By no means all of the banks have entered into direct relations with the central institution. The more important of the other banks have established close relations with some of the smaller banks, but a considerable number of the latter seem to stand entirely alone with no means of securing assistance in emergencies. It would seem that the Bank of Japan by the development of a giro-verkehr system, such as that of the Reichsbank, and in other ways might have done more to unify banking operations and to assist in the adoption of sound banking methods among the smaller banks.<sup>a</sup>

On the other hand, it must be admitted that obstacles to successful results of this sort by means of a central bank are so great as to seem well-nigh insuperable. Owing to

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<sup>a</sup>The Bank does not seem to be properly equipped for such a task. It has less than 40 officials above the rank of clerk.

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the inadequate supply of investment-capital banks in Japan, especially the small local banks are largely resorted to for more or less permanent accommodation. This condition can hardly be remedied by the Bank of Japan, which very likely is well advised in keeping clear of institutions which, though their obligations are payable on demand, employ their funds chiefly in mortgages and investment loans.

Unlike central banks elsewhere the lending business of the Bank of Japan is chiefly upon collateral security and not the discounting of commercial bills of exchange and promissory notes. A preferential rate is indeed accorded the latter,<sup>a</sup> but they have remained a comparatively small part of the total business. By the charter of the Bank direct collateral loans are restricted to those secured by government bonds and securities guaranteed by the Government. Loans secured in this way are of two kinds, loans proper and loans on current account. In the case of the latter variety a fixed maximum is agreed upon, but the borrower only pays interest upon so much of the amount as he actually uses. The number of customers having such accounts is small (51 at the head office and 98 at the branches in 1909) and the total allowed maximum is about 11,000,000 yen. The number of direct loans is surprisingly small, but 23 in 1909, a year of inactive business, and only 85 in 1908, a year of very general demand for accommodation. These loans would seem to be of a more or less permanent character, as the total in 1909, 6,970,000 yen, was only 485,000 yen less than at the end of 1908, although

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<sup>a</sup> The minimum rate is also granted upon loans secured by government bonds.

the total of loans made in 1909 was only 1,583,000 yen. Taking the two classes of secured loans together they account for about 10 per cent of the lending business, not including loans to the Government.

These loans do not by any means include all of the collateral loans made by the Bank. Bills of exchange and promissory notes must, according to the statutes of the Bank, have two indorsements, but the place of one of these may be taken by securities deposited as collateral, and the security need not be government security as in the case of ordinary loans. The annual balance sheet published by the Bank does not distinguish between bills and notes secured by collateral and those of the ordinary commercial variety. Figures are, however, published giving the total amount of the different kinds of bills discounted each year. In 1909 out of a total of 107,000,000 yen, 91,000,000 yen, or 85 per cent, were bills secured with collateral. Further analysis of these figures throws a flood of light upon the general character of the business of the Bank. These secured bills are of large average size. In 1909 there were only 320 of them taken at the head office, the average value of which was 150,000 yen, while at the branches the 864 bills taken averaged about 40,000 yen in size. These loans are the most variable element in the business of the Bank. In 1908, a year of financial strain, they reached the large amount of 489,000,000 yen, while in 1909, a year of depression, the amount discounted was only 91,000,000 yen.

Attention is called to these figures because they are an evidence of the preponderant position of the collateral

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loan in Japanese banking operations generally. Although the Bank of Japan gives the commercial bill a preferential rate its influence has not been sufficient to bring about the development of a broad commercial bill market such as is found in European countries which have central banks. The loans of the other banks in Japan are probably to an even greater extent than those of the Bank of Japan of the collateral variety, though no exact figures are available. This is not merely an impression derived from current expressions of Japanese opinion; it is an inevitable inference from the character of the business of the Bank of Japan. In seeking accommodation from the Bank the other banks would certainly make use of their commercial bills, if they had them, on account of the preferential rate. The failure to do so indicates that they must make an abundance of collateral loans and hold a comparatively small amount of commercial bills. Explanation of this situation is to be looked for in the special circumstances of the country. Japan presents striking contrasts between the most modern and the very primitive in the organization of its economic activities. On the one side there are a few large businesses most of which have taken a corporate form. In some instances the later stage of combination has already been reached. Without the many gradual steps found in other countries we go at once to the other extreme of production and distribution carried on upon an exceedingly minute scale by individuals with little business experience, making use of capital to a most insignificant extent. The economic development of the country

provides opportunities for the permanent employment of considerable capital relative to the amount available for investment in the large scale industries, the requirements of which for purely temporary purposes seem to be more than met by the existing supply of credit. Loans to small producers are not regarded favorably because of the small amount of capital which they own and because of their business inexperience. Banking funds are, therefore, employed to a very considerable extent, directly or indirectly, for long-time investment purposes in industries which have taken the corporate form.

Turning now to commercial paper proper, it may first be noted that the promissory note rather than the bill of exchange is in Japan, as in the United States, the negotiable instrument in general use for domestic transactions. In 1909 the Bank of Japan discounted only 99 domestic bills of exchange, the average value of which was in the neighborhood of 30,000 yen. In the case of promissory notes, 3,329 were taken at the head office and 3,454 at the branches, averaging in value 2,623 yen at the former and 3,108 yen at the latter. Contrasted with the total of all kinds of loans, not including those to the Government which will be considered later, the amount of these two kinds of commercial loans was less than 20 per cent at the head office in Tokyo and but 8 per cent at the branches.

Finally, in order to complete the picture of the domestic business of the Bank of Japan, the following table is appended, showing the total volume of the different kinds of loans in the successive years from 1900 to 1909.

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[Expressed in millions of yen.]

Year.	Loans to Government.	Loans on government securities.	Current accounts, maximum limits.	Bills with collateral.	Commercial bills.
1900.....	16	20	14	330	223
1901.....	62	8	12	248	129
1902.....	37	5	11	93	71
1903.....	26	2	11	91	50
1904.....	249	10	11	151	85
1905.....	244	9	11	251	51
1906.....	173	3	11	147	23
1907.....	8	8	11	374	58
1908.....	21	9	11	489	66
1909.....	27	2	11	91	16

One further line of business, partially of a domestic character, remains for examination. It appears among the assets of the balance sheet as deposits, and is a little more definitely described in the annual reports of the bank as "Loans to other banks as deposits." No indication, however, is given as to the particular banks to which accommodation is granted in this way. This item is of considerable magnitude, reaching a maximum of 52,000,000 yen in the balance sheet for 1905, but in general the amount has fluctuated between 20,000,000 and 30,000,000 yen. It includes a permanent loan of 20,000,000 yen, at 2 per cent, to the Yokohama Specie Bank, and also advances which have occasionally been made for rather long periods in connection with the rehabilitation of banking institutions which would otherwise have been forced into liquidation. The advances to the Yokohama Specie Bank should not of course be included in any estimate of the contribution of the Bank of Japan to amount of credit available for Japanese domestic industrial development.

To complete this analysis of the loans of the Bank of Japan, there remains for consideration its foreign bill holdings. These bills come entirely from the Yokohama Specie Bank and are discounted for it at the special fixed rate of 2 per cent, a rate far less than that at which any other kind of business has at any time been taken, except the permanent loan of 20,000,000 yen, also to the Specie Bank at the same rate. The domestic discount rate of the Bank of Japan was at the minimum in 1903 and in 1909 at 5.8 per cent. Market rates, it will be recalled, have been normally somewhat above bank rates. Two purposes led to the adoption of a special low rate for foreign bills. It was deemed advisable that the Bank should hold a supply of foreign bills in its portfolio in order to be able to supply exchange and thus prevent the sudden depletion of its specie reserve through gold exports. This has, however, been a matter of no importance of late years, the foreign loans of the Government during the war with Russia having provided the Bank with enormous balances in foreign countries. The low rate of 2 per cent was allowed upon rediscounts for the Specie Bank and also upon the permanent loan to it, because otherwise it would have been impossible for that bank to engage in the business of financing Japanese foreign trade in competition with the branches of foreign banks in Yokohama and Kobe. The foreign trade of the United States is almost entirely financed abroad because rates for loans are regularly higher in this country than in western Europe. There is an even greater difference between rates in Japan and those in western countries. Much unreasonable criticism has been poured out upon this practice by foreign traders in the Far East on the

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ground that it is an indirect and unfair mode of subsidizing competition. It would be more accurate to say that it merely places the Japanese on an equal footing with their competitors. If Japan is to finance any portion of its foreign trade a special rate is absolutely essential. It may, indeed, be questioned whether it is desirable (though within moderate limits it seems to be so to the writer) to employ a portion of the small available amount of Japanese capital in this way. But that it gives an unfair advantage to the Japanese trader is a conclusion which does not stand impartial examination.

The business of the Bank of Japan in foreign bills, like that of the Specie Bank, is almost entirely concerned with bills drawn against exports. Imports are still largely brought to the country by foreign firms established in the treaty ports which finance this business through the branches of foreign banks. The volume of the business in foreign bills naturally fluctuates with changes in the amount of the export trade of the country. The aggregate amount of foreign bills taken by the Bank of Japan for each year since 1900 and the amount held on balance at the close of each year are shown in the following table:

[Expressed in millions of yen]

Year.	Value of foreign bills.	Balance at close of year.
1900 . . . . .	35.1	17.3
1901 . . . . .	31.0	15.0
1902 . . . . .	34.4	13.6
1903 . . . . .	21.9	12.2
1904 . . . . .	48.6	21.5
1905 . . . . .	55.7	15.1
1906 . . . . .	42.8	23.9
1907 . . . . .	56.1	36.9
1908 . . . . .	37.6	18.4
1909 . . . . .	27.7	14.8

The loans of the Bank of Japan, like those of other central banks, fluctuate very greatly during any period of years covering a complete trade cycle. Large lending power is normally kept in reserve to be used freely to meet extraordinary requirements in periods of financial strain. In any one year, also, there are apt to be wide seasonal variations, the volume of loans being particularly great in the early autumn and at the end of the quarters of the year. As the published balance sheet of the Bank of Japan is for the end of each year, the figures which have been made use of in the preceding tables show a volume of business considerably in excess of the amount of credit which is constantly supplied by the Bank throughout any one year. Making allowance for this factor, it would seem that the Bank of Japan has added but slightly to the resources furnished through banks to the business community. Statistics bearing upon the matter are only available for the years before 1906.<sup>a</sup> The following table gives the maximum and minimum amount of loans made by the Bank of Japan in each year from 1900 to 1906:

[Expressed in millions of yen.]

Year.	Maximum amount.	Month.	Minimum amount.	Month.
1900.....	114.9	January.....	87.2	February.
1901.....	86.7	January.....	46.5	November.
1902.....	54.6	December.....	30.2	February.
1903.....	51.3	January.....	18.7	May.
1904.....	79.3	December.....	24.8	May.
1905.....	119.2	December.....	52.5	February.

<sup>a</sup> Prior to 1906 a summary of the weekly statements of the Bank of Japan was published in the *Financial and Economic Annual of Japan* issued by the Japanese government.

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Loans to the Government and loans to the banks as deposits are not included, but as the latter are largely made to the Yokohama Specie Bank, and as foreign bills are included, the table gives a fairly accurate account of the amount of loans of a purely domestic nature made by the Bank. The loans of the Bank are subject to somewhat wider fluctuations than is the case with those of European central banks. Explanation is probably found in the insignificant amount of bankers' deposits held by the Bank. Any unusual demand for cash, however small, makes it necessary for the other banks to resort to it for loans. As regards the permanent contribution of the Bank of Japan to the available supply of credit in the country, some amount between the maximum and minimum figures of the table would seem to be the proper quantity. As much as 50,000,000 yen, but certainly not more than 75,000,000 yen, may be taken as a sufficiently liberal estimate.

It would doubtless be generally agreed that the provision of a part of the credit upon which the business of the country is carried on is not one of the primary functions of a central bank. Its duties are to safeguard the banking reserve and to supply urgent requirements of an extraordinary or seasonal nature. Still, there would at first sight seem to be no good reason why the resources of such a bank should not be used within safe limits to further active enterprise rather than be invested in government bonds, the holdings of which in the particular case of the Bank of Japan have in general not been very much less than the normal volume of its domestic loans and dis-

counts. The Bank of Japan, however, probably could not have granted loans more freely with advantage to the business community and consistent with its own safety. Until the recent war with Russia the specie reserve of the Bank was hardly sufficient to permit expansion. During the period between 1900 and 1904 the issue of notes was frequently beyond the untaxed limit of 120,000,000 yen above specie holdings. Moreover, the ratio of reserve to demand obligations (deposits and notes) was during much of the time under 30 per cent, a ratio certainly not large considering the responsibilities of the Bank. Directly after the war the reserve of the Bank was much enlarged from the proceeds of foreign loans negotiated by the Government, but the extension of operations by the Bank at that time was out of the question. Rendered optimistic by successes in war and a rather fictitious abundance of capital, the business community, including most of the other banks, engaged for nearly two years in wild and reckless activities, which culminated in the latter part of 1907 in a general collapse, followed by a period of depression which has hardly reached its term at the present time.

#### THE LOANS OF THE OTHER BANKS.

While the business of the Bank of Japan has remained about stationary, that of the other banks has shown marked growth. As in other countries, the relative importance of the central bank in normal lending dealings has diminished. Elsewhere the failure of central banks to secure a constant proportion in the total volume of business has been due to the ability of the other banks to

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meet most, if not all, of the demand for loans at rates below the official rates of the central banks. In Japan, where rates of the Bank of Japan have ordinarily been below market rates, the explanation would seem to have been the inability of the central bank consistent with its own safety to have granted a larger steady volume of accommodation. The growth of the other banks is shown in the following table,<sup>a</sup> which gives the paid-up capital and surplus, the deposits and the loans and discounts of the ordinary banks, and also the savings banks, at the end of each year since 1900:

[Stated in millions of yen.]

Year.	Capital and surplus.	Deposits.	Loans and discounts of the other banks.
1900.....	293	516	716
1901.....	317	524	690
1902.....	330	621	750
1903.....	339	673	796
1904.....	338	726	816
1905.....	353	846	885
1906.....	372	1,234	1,218
1907.....	424	1,163	1,247
1908.....	447	1,153	1,231
1909.....	460	1,238	1,230

<sup>a</sup>The table does not include the agricultural and industrial banks and the Hypothec Bank, which make long-time loans with funds principally secured by the sale of debentures. The Yokohama Specie Bank, also, is not included, because its business is mostly of a special character, being concerned with the financing of foreign trade. For the sake of completeness, however, the following figures are presented for that bank:

Year.	Capital and surplus.	Deposits.	Loans and discounts.
1900.....	26.6	53.0	44.8
1906.....	34.9	120.3	97.3
1907.....	38.6	121.0	105.0
1908.....	39.5	116.8	83.6
1909.....	40.5	145.0	71.1

The extraordinary increase of the loans of these banks in 1906 calls for some notice. The war with Russia, like other wars, involved some redistribution of wealth within the country tending toward its greater concentration. The proceeds of taxes drawn from all classes are at such times paid out very largely to those furnishing supplies for the army and navy. A larger portion of the money thus secured is more likely to be lodged in banks than when it is scattered among the people at large. In the second place, there was a considerable increase in the purchasing medium within the country in the form both of notes issued by the Bank of Japan and of the proceeds of such part of the foreign loans of the Government as were brought to the country in the form of specie. Finally, it is probable that the banks themselves had strained their own credit in granting loans freely, with a consequent increase of their deposit liabilities. It should, however, be observed that this remarkable increase in loans and deposits was almost entirely held during the period of strain and depression which began in 1907.

#### THE BANK OF JAPAN AND CRISES.

The Bank of Japan found itself powerless to check to any appreciable extent the dangerously rapid expansion of credit on the part of the other banks, as well as the generally unsound and feverish economic activities which characterized the two years following the close of the war with Russia. This is a matter which would hardly deserve notice were it not for the prevalence in this country of the entirely unfounded belief that central banks are by some means able to prevent the creation of

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those unsound conditions which render crises inevitable. The Bank of Japan did keep its own resources well in hand and was able to furnish adequate assistance when the boom which followed the war collapsed, but it was able to do no more than that. The following passage, taken from the address of the president of the Bank of Japan before the meeting of shareholders in February, 1908, is most suggestive in this connection:

“With regard to economic conditions last year, a violent fall in the share market during the first half of the year produced evil effects in all directions, and although the second half witnessed a slight recovery, a panic in America and the depreciation of silver again induced a state of depression, so that the year passed amid symptoms of general dullness in the money market and in trade. From the second half of the preceding year, when the fever of enterprise rose high and when various causes contributed to aggravate it, so that share quotations attained an extraordinary level, men of judgment had already begun to look askance at the state of affairs. But as there were no means to check the trend of public feeling, it continued without abatement until the middle of January in last year. In the last part of that month, however, some factors making for a reaction showed themselves, and at once the market prices of shares displayed a disposition to decline rapidly from the abnormal heights they had reached, with the result that not a few of those concerned were involved in signal embarrassments by these vicissitudes. Nor were the effects confined to those directly interested. The banks connected

with them also felt the pinch, and various rumors being set on foot, some runs took place in the confusion. In extreme cases even banks whose condition was altogether sound saw themselves suddenly exposed to runs, and not a few were obliged to have recourse to the Bank of Japan for assistance. The Bank, having apprehended the coming of such times, had done what it could to inculcate caution by emphasizing the difference of attitude which ought to exist between those that project enterprises and those upon whom the function of supplying capital devolves. Nevertheless, things having reached this condition, mere warnings could not have much effect, and accordingly the Bank adopted the policy of rendering the necessary assistance, so far as circumstances permitted, to banks which were considered to be in a sound condition, and it carried that policy into effect in several instances. To our deep regret, nevertheless, in May and June some banks were compelled to suspend payments, because, the root of their trouble being deep-seated, no means of getting efficient succor were available."

The effectiveness of the Bank of Japan as a resource in emergencies has been exhibited on a number of occasions. There has never been any question of the power of the Bank to render all the assistance needed at such times. The problem has indeed not been one of very great magnitude. Even at the present time the loans of the other banks amount to only about 1,200,000,000 yen and their deposits to about 1,000,000,000 yen, a considerable portion of which is payable at notice. Although an extremely useful institution and rendering important services both

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to the Government and to the business community, the Bank of Japan certainly has not had to contend with problems which, relative to its resources, have had anything like the complication or difficulty of those which have at times confronted either the Bank of England or the Bank of Germany.

In handling emergencies the Bank of Japan does not take the immediate direction of affairs. Its staff is composed of officials rather than business men. It is skillful in handling monetary problems and the wider questions of policy, but is hardly well fitted to organize the particular means for relieving a strained situation. As has already been noted, the advances of the Bank are made principally to an extremely small number of borrowers. Probably the bulk of its business is with the comparatively small number of large banks, about forty in all, in Tokyo, Osaka, Kyoto, and Yokohama, whose business makes up about one-third that of all the banks. In coping with difficulties the lead is usually taken by representatives of some of these large banks and of the financial interests by which they are controlled. One example may be taken as more or less typical. In June, 1904, the One Hundred Thirtieth Bank, with head office in Osaka and thirteen branches with deposits of about 8,000,000 yen, was forced to suspend. Something like a tenth of its resources had been permanently sunk in a single enterprise, the successful issue of which could not be determined for years to come. The effect of this suspension was thus described in the Kobe Chronicle for June 30, 1904:

“When the suspension of payments by the One Hundred Thirtieth Bank of Osaka was first announced a great deal

of uneasiness was naturally aroused in banking circles in the city. Other banks sought advances from the Bank of Japan and made preparations to meet emergencies. The consequence was that advances made by the Premier Bank in Osaka increased to 10,253,000 yen on the 21st instant, but it having been soon ascertained that the effect of the suspension was confined to a small section of the business circle, the banks adopted a little easier policy, and the advances made by the Bank of Japan fell to 9,413,000 yen on Saturday last, the 23d."

The One Hundred Thirtieth Bank of Osaka was able to resume during the following month, its affairs being placed under the control of the Yasuda Bank, a loan of 6,000,000 yen having been secured for the purpose by it from the Bank of Japan. The Yasuda Bank, though an incorporated institution, is, like numbers of the other most important Japanese banks, the creation of a single man of rare business capacity. This particular bank has been especially active in the rehabilitation of banks and other companies which would otherwise have been forced into liquidation and bankruptcy. Operating in close relation to the Bank of Japan, results have been accomplished which would probably never have been attempted by the Bank upon its own initiative.

#### THE INFLUENCE OF THE BANK OF JAPAN ON RATES FOR LOANS.

One of the results expected from the establishment of the Bank of Japan was the lowering of the extremely high rates then prevailing for banking accommodation. Whether the operations of the Bank have had any very

pronounced effect in this direction can not be determined with certainty. Judging from the comparatively small amount of loans regularly made by the Bank it might seem that its influence must have been very slight. On the other hand, it is certain that the presence of the Bank has diminished the tendency of rates to advance to extremely high levels in periods of seasonal or extraordinary strain. This is in itself a very great gain. Indeed, it is evidence of the successful performance by a central bank of its primary function on the banking side. It is also possible that the operations of the Bank of Japan, by diminishing for other banks the risks arising out of general causes to which the business is subject, may have fostered the investment of capital in banking.

An examination of the actual course of rates for loans does not enable one to determine the effect upon them of the single influence of the Bank of Japan. Too many other influences were at work. Rates for loans reached about as high levels in 1898 as in 1882 before the establishment of the Bank and were not much less at any time during the first fifteen years of its history than they were in 1883. Throughout this period the minimum rates at which the Bank of Japan granted accommodation ranged from two-fifths of 1 per cent to more than 1 per cent above minimum market rates and there was in each year an even greater discrepancy between the maxima of these rates. Since 1900 a new situation of affairs is beginning to make itself apparent. Market rates have at times in every year since 1903 ruled below the official rates of the Bank of Japan. It is still true, however, that market rates in all

of these years have been above bank rates during a part the time. But evidently the Bank is approaching in this respect the situation of similar institutions in other countries. It may be predicted with confidence that in the not distant future the rates of the Bank will be normally above, occasionally at a level with, market rates and practically never below them. Rates are still high in Japan judged by western standards. In 1909 a discount rate of 4 per cent was for the first time quoted in Tokyo. The rates of the Bank of Japan have never been less than 5.8 per cent, and during the last ten years the maximum discount rate has been between 8.8 per cent and 6.2 per cent. Seven and three-tenths per cent may be taken as a fair average.<sup>a</sup>

Another expectation from the establishment of the Bank of Japan was the equalization of rates throughout the country. This was not realized during the first twenty years of its history. The bank lent at different rates at its various branches and charged a premium on exchange to prevent the proceeds of loans made where its rate was low from being transferred to localities where its rate was high. In 1906 this practice was changed, apparently not as a result of anything which had been accomplished by the bank itself but, because with the development of banking facilities furnished by other banks, rates had of themselves become more even throughout the country.

At the outset it was stated that the operations of the Bank of Japan seemed especially worthy of study by Americans, because they presented the only instance of

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<sup>a</sup> Rates for loans in Japan are quoted in sen for 100 yen for one day.

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a central bank working among a numerous company of other banks. It will, however, have been observed that the experience of the Bank affords little or no indication of the probable results from the establishment of a central bank in this country. Public opinion is not as yet a powerful force in Japan, and in particular it does not concern itself with banking matters. The Bank has been free to confine itself to a comparatively small number of borrowers, far less than the total number of banks, and has been under no pressure to extend its credits in periods of active business. Moreover, relative to the total of credit operations of all of the banks, the Bank of Japan has kept a sufficiently large lending power in reserve so that it has been able to meet periods of financial strain without difficulty. Relative to its resources the banking problems with which it has been concerned have not been of anything like the magnitude of those which have confronted such central banks as those of England and Germany. Further, the chief preoccupation of the bank has been of a monetary rather than a banking nature. It rendered great service in 1897 when Japan changed from the silver to the gold standard, and it has skillfully protected the specie foundation of the monetary and credit fabric from disturbance through specie exports. In fact, aside from emergencies, it is rather as an organ of the Government in relation both to the monetary system of the country and the government finances that the Bank may be said to have rendered its greatest service and not as a part of the banking system of the country.

## THE BANK OF JAPAN AND GOVERNMENT FINANCES.

The utility of the Bank of Japan to the Government was strikingly shown in the course of the war with Russia between February, 1904, and September, 1905. At the outset the Government borrowed largely from the Bank, its loans to the Government, including its holdings of government bonds advancing from 43,000,000 yen in December, 1903, to 116,000,000 yen at the end of 1904. Some increase, which may also be attributed to activities connected with the war, took place in the other loans of the Bank. Its entire lending power was put to use in the course of the first months of the contest. Its note issue was increased by 54,000,000 yen to 286,000,000 yen, and was then 83,000,000 yen in excess of the untaxed limit. At the same time its specie reserve fell from 113,000,000 yen to 83,000,000 yen and was only 25.5 per cent of its demand liabilities. The bank had evidently exhausted its lending power. The financial situation both of the Government and of the Bank was placed upon a more secure footing in 1905 by means of the foreign loans negotiated by the Government. The loans of the Government to the Bank were reduced by 46,000,000 yen while government deposits were increased from 33,000,000 yen to 438,000,000 yen. This enormous increase was reflected on the other side of the account of the Bank chiefly in balances abroad which amounted to 373,000,000 yen, by an increase in specie holdings of 33,000,000 yen. There was also a further increase in note issue of 26,000,000 yen. The large government balances were, of course, much reduced during the remainder of the war and immediately thereafter. At the same time the

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foreign balances of the Bank had been reduced, but by no means to so great an extent. During the four years to the end of 1909 government balances were reduced by 250,000,000 yen while foreign balances of the Bank were reduced by only 145,000,000 yen. Evidently the Government must have used a part of its funds secured in foreign countries in making payments in Japan. This will explain the increase in specie holdings of the Bank by 102,000,000 yen during the four years, which gave the Bank at the end of 1909 a specie reserve of 218,000,000 yen. This increase is partly accounted for by a reduction of loans to the Government and government bonds held by the Bank amounting to 55,000,000 yen, and, further, by an increase in note issue of 40,000,000 yen.

### CONCLUSION.

The total increase of the note issue from 232,000,000 yen in 1903 to 352,000,000 yen at the end of 1909 was in large measure a result of financial transactions with the government arising out of the war. But the present supply of notes does not seem to be excessive; it represents in large measure Japan's share in the increasing gold supply of the world. Like the Bank of France the Bank of Japan has been strengthened through the exchange of gold for its notes which is due to the preference of the people for a paper circulating medium. Like the Bank of France, also, the Bank of Japan has not increased the normal volume of its loans because of this increase in its gold holdings. The Bank is now in position to aid in the development of the country by judicious advances to a far greater extent than was possible for it at any time in the

past. If this policy should be adopted the problem of handling the loan account of the Bank will probably become far more complex than ever before. Loans in large volume to other banks at rates less than those exacted by them from individual borrowers would seem to be neither possible nor desirable. The time is, however, still distant when the Bank will experience that difficulty in making its rate of discount effective which has been encountered by European central banks. It would seem probable that an increase in its loans to individual borrowers in normal times would enable the bank to restrain excessive credit expansion in years of unhealthy speculative activity. By contracting its own loans at such times, the demand for accommodation at the other banks would be increased and many of the more undesirable loans would probably be refused.

In conclusion, it may be repeated, the experience of the Bank of Japan, while interesting in itself, does not yield much in the way of guidance for this country. Differences in political organization and in the influence of public opinion could hardly be more extreme. The foreign exchange position of the two countries is quite unlike. It is altogether unlikely that a United States central bank would lend at rates below those of the other banks, since the supply of credit is already ample for all ordinary requirements. And finally it should be noted that the credit structure of the other banks relative to that of a central bank would be so many many times greater in the United States than it is in Japan as to make the problem which would confront its management and the methods which would prove effective entirely different in character.









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